

BEFORE THE OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

IN THE MATTER OF THE APPEAL OF,)
)
K. BABAOFF and S. BABAOFF,) OTA NO. 19125534
)
)
 APPELLANT.)
)
)
 _____)

TRANSCRIPT OF ELECTRONIC PROCEEDINGS

State of California

Wednesday, January 25, 2022

Reported by:
ERNALYN M. ALONZO
HEARING REPORTER

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25

BEFORE THE OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

IN THE MATTER OF THE APPEAL OF,)
)
K. BABAOFF and S. BABAOFF,) OTA NO. 19125534
)
) APPELLANT.)
)
)
_____)

Transcript of Electronic Proceedings,
taken in the State of California, commencing
at 2:51 p.m. and concluding at 3:38 p.m. on
Wednesday, January 26, 2022, reported by
Ernalyn M. Alonzo, Hearing Reporter, in and
for the State of California.

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25

APPEARANCES:

Panel Lead: ALJ AMANDA VASSIGH

Panel Members: ALJ RICHARD TAY
ALJ JOSHUA LAMBERT

For the Appellant: ROBERT CORBIN
ERIC BLAU
K. BABAOFF

For the Respondent: STATE OF CALIFORNIA
FRANCHISE TAX BOARD

DAVID HUNTER
MARGUERITE MONET

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25

I N D E X

E X H I B I T S

(Appellant's Exhibits 1-6 were received at page 7.)
(Department's Exhibits A-M were received at page 7.)

OPENING STATEMENT

	<u>PAGE</u>
By Mr. Corbin	8

PRESENTATION

	<u>PAGE</u>
By Mr. Blau	10
By Mr. Hunter	19

WITNESS TESTIMONY

	<u>PAGE</u>
By Mr. Babaooff	13

CLOSING STATEMENT

	<u>PAGE</u>
By Mr. Corbin	28

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25

California; Wednesday, January 26, 2022

2:51 p.m.

JUDGE VASSIGH: We are opening the record in the Appeal of Babaoff. This matter is being held before the Office of Tax Appeals. The OTA Case Number is 19125534. Today's date is Wednesday, January 26th, 2022, and the time is 2:51 p.m. This hearing is being conducted electronically with the agreement of the parties.

Today's hearing is being heard by a panel of three Administrative Law Judges. My name is Amanda Vassigh, and I will be the lead judge. Judges Lambert and Tay join me as members of this panel. All three of us will meet after the hearing and produce a written decision as equal participants. Although, I will conduct the hearing, any judge on this panel may ask questions, or otherwise participant to ensure that we have all the information we need to decide this appeal.

For the record, will the parties please state their names and who they represent, starting with the representatives for the Franchise Tax Board.

MR. HUNTER: David Hunter, Franchise Tax Board.
Thank you.

MS. MONET: Marguerite Monet, Franchise Tax Board.

1 JUDGE VASSIGH: Thank you. This is Judge
2 Vassigh. Can representatives for the Appellant please
3 state their names.

4 MR. CORBIN: Yes. This is Robert Corbin, CPA
5 from Windes.

6 MR. BLAU: This is Eric Blau, CPA. Also from
7 Windes representing the Appellant.

8 JUDGE VASSIGH: Okay. And I notice that one of
9 our Appellants is on the line. Can you please state your
10 name, please.

11 MR. BABAOFF: Kambiz Babaoff, Appellant.

12 JUDGE VASSIGH: Thank you.

13 This is Judge Vassigh again. Appellants
14 indicated in our prehearing conferences that they would
15 call Mr. Babaoff as a witness today.

16 Mr. Babaoff, when we're ready I will swear you
17 in.

18 MR. BABAOFF: Okay.

19 JUDGE VASSIGH: Okay. So we'll review exhibits
20 now. The parties have emailed the electronic exhibits
21 binder. The exhibits for this appeal have been admitted
22 into evidence without objection and consist of; for the
23 agency FTB's exhibits numbered A through M; and for the
24 taxpayer we admitted Exhibits 1 through 5, plus the
25 addition today. We will now admit Exhibit 6.

1 I will reiterate on the record that the panel
2 will not treat any recitations of law or legal analysis
3 contained within exhibits as fact. But Appellants and the
4 agency may refer to the law or include any relevant
5 information in their presentation.

6 Earlier the parties indicated no objections and,
7 therefore, the evidence is now admitted into the
8 evidentiary record.

9 (Appellant's Exhibits 1-6 were received
10 in evidence by the Administrative Law Judge.)

11 (Department's Exhibits A-M were received in
12 evidence by the Administrative Law Judge.)

13 And we will move on to the issues to be heard in
14 this appeal. The issues to be decided in this case are:
15 One, whether Appellants have shown they're entitled to a
16 claimed capital loss of \$3,250,000; and two, whether
17 Appellants are liable for the accuracy-related penalty.

18 As a reminder to the parties, during our
19 prehearing conference, we decided that Appellants will
20 have up to 20 minutes to make their opening presentation.
21 Then the parties will each have up to 25 minutes to make
22 their arguments and present witness testimony. And at the
23 end Appellants will have 5 minutes, if they choose, to
24 provide a rebuttal argument.

25 Does anyone have any questions before we move

1 onto opening presentations?

2 MR. CORBIN: No.

3 JUDGE VASSIGH: We are ready to proceed with
4 Appellants' opening presentation. When you are ready,
5 please begin.

6

7

OPENING STATEMENT

8 MR. CORBIN: So Your Honor and Judges, this is
9 Robert Corbin from Windes, Inc., representative of Kambiz
10 Babaoff and the issue at point.

11 We intend to discuss the relevant legal language
12 and analysis under the tax law of California to discuss
13 the deduction that is under issue. We intend to provide
14 relevant case law. We intend to provide testimony from
15 Mr. Kambiz Babaoff, as far as his experience during the
16 issue at hand and the discussion of the deduction, also,
17 the dollar amount and how that was ascertained, and the
18 concepts related to why that would be allowed relevant
19 to -- why that would be allowed relevant to the questions
20 that were achieved with the Franchise Tax Board.

21 The important thing to realize on this opening
22 statement is to realize that we have the documentation
23 that derives the income number. We have representation of
24 Kam and the documentation relative to the timing of the
25 deduction. The legal analysis relative to why we took the

1 deduction and why it was allowed.

2 We will through a number of different cases
3 through my colleague Eric Blau who will represent the
4 legal aspect of that -- those cases and why they are
5 pertinent to this. In addition, that representation will
6 be a foundation of the penalty removal, for the
7 accuracy-related penalty. We believe that we have done
8 our due diligence. We've done our background dissertation
9 and analyzed the numbers that Mr. Babaoff had given to us
10 to remove the implication of an accuracy-related penalty.

11 That's it.

12 JUDGE VASSIGH: This is Judge Vassigh. Thank
13 you. Would you like to presented your witness now?

14 MR. CORBIN: We'd actually like to go into the
15 legal arguments of the case law related to the
16 availability of the deduction prior to calling
17 Mr. Babaoff.

18 JUDGE VASSIGH: Okay. Let me know when you're
19 ready to call Mr. Babaoff, and I will place him under
20 oath. And please go ahead and start your arguments.

21 MR. CORBIN: So I'd like to turn this over to
22 Mr. Eric Blau who did a significant amount of research
23 related to the case law that's applicable to this case;
24 the dollar amount, our representations, the timing, and
25 why it was pertinent to take appropriate deductions in the

1 year it was taken.

2

3

PRESENTATION

4

MR. BLAU: Hello. This is Eric Blau.

5

6

7

8

9

10

11

12

13

14

15

16

17

18

19

20

21

22

23

24

25

It seems that many of the issues that have been brought up related to the deduction surround the issue of documentation. So we would start by showing that there was continued ownership within the property that's in question, and the taxpayer consistently stated that he held the property in hopes to sell. There was a final confirmation of confiscation that was provided by the taxpayer via email, which to the best of his knowledge and good faith efforts, reflect that the property was taken in September of 2011 in which he deducted the loss in 2011.

The taxpayer's testimony of his intent to sell to the local authorities is basically what had led to the confiscation, and the FTB even acquiesce that Mr. Babaoff did, in fact, own the property. So as far as trader business income, there is a case, the State of Miller, in which case the owners of a property had an intent to sell. They did not use the property for personal use, and the deduction on the sale was actually a taxable deduction. And so the taxpayer ultimately had an end goal, and it was substantiated in the Miller case to the extent that they held the property for profit.

1 So in other words, the code does not actually get
2 into what "holding for profit" actually means. And so
3 when we looked for guidance, the only place that we can go
4 is this specific case. There is also another case Salt v
5 Commissioner in which case the property was confiscated.
6 The owner of the party had no income related to that
7 property, and they were also allowed to substantiate the
8 deduction.

9 So in both cases we have similar facts. In our
10 case the property was inherited. That is similar to the
11 Miller case. The Salt case the property was confiscated.
12 In both cases there was no income and the deduction was
13 substantiated. So to me I think that we do get there in
14 terms of whether the property was held for profit. The
15 taxpayers clearly intended that they had a goal of selling
16 the property, which is what led to the confiscation. So
17 to me I think that we do get there in terms of holding for
18 trade or business.

19 So the next is, if that -- if we can say that the
20 property was deductible, the next question is the question
21 of what the tax basis of the property was. And under
22 Rule 84139, it's very clear that a U.S. person does
23 receive a step-up for property that is inherited, even if
24 it's a foreign property from a foreign person. Further,
25 to the extent that the loss is deductible, and we don't

1 have sufficient amounts of documentation, we can use the
2 Cohan rule. And that was alluded to in the Salt v
3 Commissioner case in which they actually did use the Cohan
4 rule to come up with what the basis of the property was.

5 So to me I think that we have -- we have the
6 substantiation to take the loss. We have made our best
7 estimates of what the cost basis of the property was. We
8 have documentation that shows the actual confiscation had
9 occurred in 2011, and that was provided. And we've -- we
10 have proven that the property was, in fact, held for a
11 profit motive as it was never used as a personal property.

12 And that's all I have.

13 JUDGE VASSIGH: This is Judge Vassigh. Thank
14 you, Mr. Blau.

15 Would you like to present witness testimony from
16 Appellant at this point.

17 Mr. Corbin, you're on mute.

18 MR. CORBIN: I would like to introduce
19 Mr. Kambiz Babaoff as the witness, the taxpayer who can
20 provide some additional information regarding his factual
21 pattern about what happened to the property and how it
22 dovetails into our taking of the deduction.

23 JUDGE VASSIGH: Thank you, Mr. Corbin. This is
24 Judge Vassigh.

25 Mr. Babaoff, I will place you under oath now so

1 we can consider your statements as testimony, and you will
2 remain under oath until the close of this hearing.

3 Please raise your right hand.

4

5 KAMBIZ BABAOFF,

6 produced as a witness, and having been first duly sworn by
7 the Administrative Law Judge, was examined and testified
8 as follows:

9

10 JUDGE VASSIGH: Thank you, Mr. Babaoff. You may
11 proceed.

12

13 WITNESS TESTIMONY

14 MR. BABAOFF: Thank you very much for the
15 opportunity to speak here this afternoon.

16 Your Honors, by way of background I came to this
17 country in 1976 to attend college in Los Angles. I
18 started at USC to study engineering with the intent of
19 going back to Iran and join my family in the business.

20 JUDGE VASSIGH: I'm sorry. This is
21 Judge Vassigh. I'm so sorry to interrupt you,
22 Mr. Babaoff. Is it possible to get closer to your
23 microphone?

24 MR. BABAOFF: Yes, I can. Is this better?

25 JUDGE VASSIGH: Yes, that is.

1 Ms. Alonzo, is that better for you too? I just
2 want to make sure we capture everything.

3 MR. BABAOFF: Should I repeat that, or did you
4 hear what I said.

5 JUDGE VASSIGH: Ms. Alonzo, does he need to
6 repeat it? No. Okay. Thank you.

7 MR. BABAOFF: As we all know the revolution
8 happened in Iran in 1979 followed shortly thereafter by
9 the takeover by the U.S. Embassy and the hostage crisis,
10 for those of you who were there at that time. My family
11 being associated with the previous regime and of Jewish
12 heritage had to escape the country.

13 My father and I started our development company
14 from scratch. We, basically, had no money at the time in
15 1979, October of 1979. We built the business over the
16 next several years until he retired, and I continued in
17 the development and management of various kinds of real
18 estate that currently employs almost 1,000 people
19 directly. I consistently contribute to nonprofit within
20 our community. And using my development skills, I'm
21 chairing an organization called Corner Stone for housing
22 for adults with disabilities; that build affordable
23 housing for young adults with disabilities.

24 With respect to this particular property in
25 question, it was inherited by me when my grandfather

1 passed away in 1977 while I was in the U.S. My cousins
2 and I each received one-fourth share in the property.
3 This property was land that was owned by my grandfather
4 outside of town that we used to go to -- it's sort of a
5 farm -- when we were growing up. And throughout the
6 years, it became very much in town, and zoning allowed
7 high-rise development construction on the side.

8 We, meaning my cousins and I, planned to return
9 to Iran and sell the property. No owners resided at the
10 property after the death of my grandfather. One of my
11 uncles, who was a dentist at that time, went back to
12 Tehran in 2008, 2009, and started talking to some brokers
13 with respect to selling the property. When the Islamic
14 Republic was notified that one of the owners had returned
15 to sell the property, they immediately put a hold on the
16 title and moved to confiscate the property.

17 I believe they used the same allegation they used
18 on my father for confiscating all of his assets as being
19 Zionist Sympathizers. The process was bureaucratic.
20 Multiple agencies worked to confiscate the different
21 ownership pieces, which was mine and my cousin as
22 indicated in the Letter of Confiscation. I don't know
23 exactly the reasoning behind that, but maybe to make it
24 more legitimate.

25 It is my understanding that the property was

1 officially taken from us in 2011, at which point, I
2 immediately had an appraisal done of the property of the
3 value at the time and converted it to U.S. dollars, the
4 exchange rate at the time. The currency, just for your
5 information, has devalued 4,000 percent since the
6 revolution in 1979. As such I believe our valuation on
7 the property was very conservative.

8 This concludes my statement. I'm happy to answer
9 any questions.

10 JUDGE VASSIGH: This is Judge Vassigh. Thank
11 you, Mr. Babaoff for your statement and for sharing that
12 history with us.

13 MR. BABAOFF: Thank you.

14 JUDGE VASSIGH: I'd like to ask my fellow
15 panelist if they have any questions. Judge Lambert, do
16 you have any questions?

17 JUDGE LAMBERT: This is Judge Lambert. I don't
18 have any questions at this time. Thanks.

19 JUDGE VASSIGH: Thank you.

20 Judge Tay do you have any questions?

21 JUDGE TAY: Just one question for the witness.
22 Mr. Babaoff, what was the property used for before your
23 grandfather passed away, and what was it used for
24 subsequent to that?

25 MR. BABAOFF: It was, basically, a land with some

1 structure on it that was for developmental purposes in the
2 future. It was, basically, agriculture land that became
3 part of the -- inside the zoning of the property and
4 became development property.

5 JUDGE TAY: I'm sorry. That was?

6 MR. BABAOFF: It became developable. At that
7 time we were just -- they were just nothing. It was just
8 land, as the landholder.

9 JUDGE TAY: I see. Okay. Thank you. I have no
10 further questions.

11 MR. BABAOFF: Thank you.

12 JUDGE VASSIGH: Okay. I'd like to see if
13 Mr. Hunter or Ms. Monet have any questions for the
14 witness.

15 MR. HUNTER: Hunter here. No questions from me,
16 Judge.

17 MS. MONET: This is Marguerite Monet. I don't
18 have any questions.

19 JUDGE VASSIGH: Thank you very much.

20 This is Judge Vassigh. Again, I do have a
21 question first for Appellant's representatives. I would
22 like to understand. It seems that you're arguing that the
23 date of confiscation is the date that the decree was
24 translated; is that correct?

25 MR. CORBIN: Yes. I think there was a number

1 of -- in the background before the actual determination of
2 the date of deduction that we took on the tax return. As
3 Mr. Babaoff has mentioned, there was a number of
4 administrative arguments and push back related to the
5 Iranian government as they tried to maintain the ownership
6 of the property. And, ultimately, there was communication
7 in 2011 that it was pretty final and determinative that
8 this property was going to be taken from Mr. Babaoff.

9 JUDGE VASSIGH: Okay. So you're saying that it
10 was not until 2011 that the decree was final.

11 MR. CORBIN: Correct. That was the year we took
12 the deduction. Correct.

13 JUDGE VASSIGH: Okay. Because there seem to be
14 some argument about the date of translation.

15 MR. CORBIN: Well, if I can refer to Mr. Babaoff
16 to add some color to the analysis and fight regarding the
17 absorption of the property and what was done prior to
18 2011. Because when we included it on the tax returns as a
19 deduction, it was our understanding that those arguments
20 were final at that point. There was no other way to go.
21 It wasn't in 2010, and it wasn't going into 2012.

22 JUDGE VASSIGH: Mr. Babaoff, can you add some
23 clarity about the date of the decree and when confiscation
24 was final in your mind?

25 MR. BABAOFF: The decree happened in writing by

1 the Court Islamic Authority. They have different agencies
2 that they use to people's property outside the country.
3 And my portion of the property was expropriated, people's
4 property that are outside of the country. And my portion
5 of the property was expropriated by -- I don't remember
6 the name of the agency. It's in the translation.

7 But the actual decree issued in 2011. I don't
8 know the exact month. And at the time that we received it
9 in writing, then we submitted it for official translation.

10 JUDGE VASSIGH: Okay. Mr. Babaoff, do you read
11 Persian?

12 MR. BABAOFF: Yes, I do.

13 JUDGE VASSIGH: Okay. So you were just waiting
14 for the official translation, but you did understand the
15 correspondence?

16 MR. BABAOFF: Yes.

17 JUDGE VASSIGH: Okay. All right. So if there
18 are no other questions by the panel, we can move on to the
19 Franchise Tax Board's presentation. Please begin when
20 you're ready.

21

22 PRESENTATION

23 MR. HUNTER: Thank you, Judge. My name is David
24 Hunter. And also on the screen with me, as we said, is
25 Marguerite Monet from the Franchise Tax Board.

1 This case involves an expropriate loss in the
2 amount of \$3.2 million as reported for tax year 2011.
3 Appellant reported that this loss was being used to offset
4 capital gain of \$14 million from the sale of his other
5 investment properties. The operative statute here is
6 Internal Revenue Code Section 165. In order to properly
7 claim this loss, Appellant must prove the following with
8 contemporaneous and credible evidence.

9 One, his ownership of the property in question;
10 two, that this property was used in a trade or business
11 entered into for profit; three, actual management and
12 control at the time of confiscation; four, the
13 unquestionable application of a confiscatory action by the
14 foreign government, meaning the foreign government
15 obtained title to the property; five, the date the
16 confiscation occurred; and finally, six, his adjusted
17 basis in the property.

18 And in this case, Appellant failed to do so on
19 all points. For example, Appellant failed to -- his own
20 evidence as he presented, lays out several inconsistent
21 and irreconcilable accounts of how he came into the
22 ownership of this claimed property interest. While it's
23 true FTB agreed that he owned the property at one time, in
24 one document he provided he claims he inherited his
25 interest in the property many, many years ago, sometime

1 between 1977 to 1979, while in another, he claims he
2 received the property via gift.

3 That's from his grandparents along with some of
4 his cousins at a time prior to 1976. And this is
5 important because both of these scenarios have different
6 outcomes when it comes to establishing tax basis or
7 adjusted tax basis on the property. Internal Revenue Code
8 Section 165(a) and subsection (b) provide that the amount
9 of the loss of deduction is the adjusted basis under
10 Internal Revenue Code Section 10111, which means that you
11 have to account for the basis when the taxpayer received
12 the property and also account for depreciation over the
13 years.

14 Here, instead, Appellant provided a document
15 allegedly written by a government official to establish
16 the fair market value of the property, maybe in 2011, but
17 it's not clear what year he obtained this appraisal for.
18 And also, there's no layout of how this appraisal was
19 calculated. There's no comps or comparable properties at
20 issue.

21 Next, Appellant provided two documents that he
22 claims are Official Pronouncements of Confiscation by the
23 Iranian government. It should be noted that these
24 documents are purportedly from officials located in a
25 foreign country and, thus, don't have a presumed

1 credibility of official records here in the United States.
2 One document explains that his interest in the property
3 was acquired by the Iranian government via
4 Order Number 251/324 issued on May 10th, 1983, by the
5 Revolutionary Court of Iran. That's Exhibit 1.

6 Another document explains that his interest in
7 the property was acquired by the Iranian government for
8 the same order, Verdict Number 251/324 dated May 31, 2011.
9 That's Exhibit 4. We're talking about the same order, but
10 somehow, they were entered 20 years apart. Also, the
11 documents provided infer that Appellant may have been, in
12 fact, compensated for his property interest. It reads,
13 "It has been irrevocably transferred to Appellant, 52
14 million rials, equivalent to \$753,000 U.S. dollars back on
15 October 6th, 1976." That's Exhibit 4.

16 Here it's beyond dispute that Appellant has not
17 demonstrated that he maintained this property since he
18 moved to the United States in 1976. In his narrative he
19 acknowledges that a lien was placed on his portion of the
20 property, and he acknowledges that he did not pay
21 attention to the property for years. The bottom line is
22 Appellant failed to show any of the required elements to
23 deduct this confiscation loss in the amount of 3 and a
24 quarter of a million dollars.

25 He hasn't shown that he held the property in the

1 course or of the trade or business or held it in
2 investment. He has not made a proper showing as it
3 relates to the accounting issues, and he has not
4 substantiated that 2011 is the proper year to report the
5 loss.

6 What we are looking for here? The case that we
7 have in our brief is Soukkanian. It's referred to by both
8 parties. In Soukkanian, the issue of ownership was not in
9 dispute. The issue of continued ownership, management,
10 and control was not in dispute because the taxpayer had a
11 family member and an agent that was taking care of the
12 property. In Soukkanian, there were two properties at
13 play. One was a villa, which was a residential property,
14 and that portion of the expropriation loss was disallowed
15 because the taxpayer could not show it was used in a trade
16 or business entered into for profit. It was a residence.

17 The other property, a portion of the loss
18 deduction was allowed because the bottom floor of this
19 apartment building was used as a residence. However, the
20 other units above were, in fact, rented out, and they had
21 rental agreements and bills that were associated with the
22 property. That was an ongoing concern.

23 We don't have that here. And if we can talk
24 about the late submission, we have a couple of cases. One
25 is Miller. That stands for the premise where a taxpayer

1 inherits the entire title or interest of a property that
2 they previously held under joint tenancy, here a husband
3 and wife. If they can show that property was used in a
4 trade or business, well then, the loss deduction would be
5 allowed -- strike that.

6 The deduction would be allowed. The property
7 would be considered that it was used in a trade or
8 business as opposed to a personal residence. Forgive me,
9 but that was the call of the question in that case. The
10 husband passed away. The wife inherited the property.
11 She had the entire interest. It was used as their
12 vacation home even though it was a residence. And even
13 though the property did not sell right away, she was able
14 to show continued ownership, and the property sold three
15 years after it was listed.

16 That was the only issue that was raised in that
17 case, and I feel that it was correctly decided. But that
18 case does not apply to the facts in this case where the
19 taxpayer cannot show continued ownership and control in
20 the first place. Same thing with the other case that was
21 introduced this morning. Salt, that was a case along with
22 Miller where facts were stipulated, not the facts that are
23 at issue in this case. And in Salt, again, the taxpayer
24 was able to show continued management and control over the
25 property at issue. He had a family member manage the

1 property, as well as a farm hand.

2 There was no issue as to the date of confiscation
3 by the Hungarian government. The taxpayer was able to
4 prove that the United States declared war in 1942, and the
5 Hungarian government confiscated his property in 1945. In
6 that case the court did employ the Cohan rule. Why?
7 Because they found that the taxpayer, the lack of a
8 concrete number was not due to an exactitude of his own
9 making. And they have a basis upon which to calculate the
10 number, which would be his adjusted basis. I believe it
11 was maybe \$7,500 in that particular case.

12 So while the cases that were introduced this
13 morning do present some basic tenants of law under
14 expropriation laws in Section 165, they don't do anything
15 to shed any more light on the facts in this particular
16 case. We still have a lot of questions, and we don't have
17 credible and contemporaneous evidence on all of the
18 factors needed to support this deduction, again, as
19 reported and in the year that it was reported.

20 Finally, as a way it relates to the
21 accuracy-related penalty, Revenue & Taxation Code
22 Section 19164 provides for a penalty of 20 percent when
23 taxpayers understate their taxable income by more than
24 10 percent or \$5,000. Here, it was based on a substantial
25 underpayment and mechanically applied because the tax

1 required to be shown on the return is \$616,000.
2 10 percent of this amount is \$61,000, and the amount of
3 the understatement is \$334,000, therefore, exceeding
4 \$61,000 by a substantial amount.

5 In this case, we don't have evidence that will
6 support a defense of reasonable cause. Appellants have
7 not briefed it, and they provided no legal basis to abate
8 this penalty.

9 So based on the foregoing, we feel our action
10 should be sustained. Thank you.

11 JUDGE VASSIGH: Thank you, Mr. Hunter. I'd like
12 to see if my co-panelists have any questions for you.

13 Judge Lambert, do you have any questions?

14 JUDGE LAMBERT: This is Judge Lambert. I have no
15 questions. Thanks.

16 JUDGE VASSIGH: Thank you.

17 Judge Tay, do you have any questions?

18 JUDGE TAY: Just one question of clarification
19 for Mr. Hunter. You mentioned that the Appellant appears
20 to have received some compensation for some transaction or
21 property that occurred in the 70s; is that correct?

22 MR. HUNTER: Yes. One of the documents made
23 mention of him receiving \$700 -- strike that -- the
24 equivalent of \$753,000 back in 1976. That is correct,
25 Judge Tay.

1 JUDGE TAY: And what are we -- how can we
2 interpret that? Or what effect does that have given that
3 the date of actual confiscation might have been sometime
4 in the 80s or 2011.

5 MR. HUNTER: Well, your guess is as good as mine.
6 I mean, if he inherited this property, then we would have
7 to establish, one, the date of the inheritance. We'd have
8 to establish the fair market value at that time, and then
9 we can track that going forward. If he was compensated
10 when the property was expropriated by a foreign
11 government, well then there's really no loss because he
12 received money.

13 And, again, this is just a statement in the
14 document that was presented. And I offer that to say that
15 these documents they have these inherent unreliability
16 factors in them because you wouldn't be able to report a
17 confiscation loss if you received compensation for the
18 property that you claim was taken from you.

19 That's why I brought that up.

20 JUDGE TAY: Okay. Thank you. No further
21 questions.

22 JUDGE VASSIGH: This is Judge Vassigh. At this
23 point I'd like to offer Appellant and his representatives
24 the opportunity to provide a rebuttal to Franchise Tax
25 Board's presentation, if you would like to take that.

1 accountants on hand during that period of time that had
2 not -- did not -- were involved in the actual discussion
3 and/or argument with the Iranian government regarding the
4 absconding of the property.

5 And so from our perspective, we believe that the
6 deduction was allowable during the period when he received
7 the document from the Iranian government that said this is
8 final dissertation about taking the property, and there
9 was no other way to do it. So 2011 was the year to take
10 the deduction.

11 And so maybe I can turn it over to Mr. Babaoff to
12 discuss his understanding about remuneration that has been
13 brought up prior to -- in 1977 relative to his ownership
14 of this property. Because if the remuneration was taken
15 by his uncle, and was included in his uncle's return, I
16 would bet he would not be subject to California Franchise
17 Tax at that time. It would not be irrelevant to
18 Mr. Babaoff's increasing basis on the inheritance and the
19 ultimate deduction that we took about the capital loss on
20 2011.

21 So, Kam, if you could --

22 MR. BABAOFF: I think the document Mr. Hunter is
23 referring to and refers to remuneration at the time in
24 1976. I think that's the valuation of the property, not
25 remuneration of the property in that time because we were

1 asked what the value of the property was at the time that
2 it was inherited and the basis of the property. And we
3 went back and received documents that would value the
4 property or the basis of the property at the time.

5 It wasn't meant that that was the value that we
6 actually received. It means that what we receive, that's
7 the value of the property that was inherited at the time.
8 It wasn't like we received the cash. That's the valuation
9 to put on the property, the so-called basis at the time.

10 MR. CORBIN: Okay. And then secondly, is that
11 even if that was the valuation of the property at the
12 time, the ultimate decision and finality of the
13 transaction occurred in 2011. So the value was not
14 indicative of the determination at 1977 but most likely at
15 the date of the finality by the Iranian government. We
16 would take the ultimate step-up in basis and deduction
17 relative to that valuation.

18 I'd like to move to Mr. Blau to add some color to
19 the accuracy-related penalty.

20 MR. BLAU: So Jack, can you hear me?

21 MR. CORBIN: Yes.

22 MR. BLAU: This is Eric here.

23 So generally the most important factor for the
24 accuracy-related penalty is the taxpayer's effort to
25 assess the proper tax liability. Circumstances that may

1 indicate reasonable cause and good faith are an honest
2 misunderstanding to the fact of law that is reasonable in
3 the light of all facts and circumstances, including
4 experience, knowledge, and education of the taxpayer.

5 And isolated computational or transcriptional
6 error, generally, is not inconsistent with reasonable
7 cause in good faith. So I'm citing Reg Section 1.6664-4,
8 which basically states that we put our best faith -- good
9 faith effort into computing what the tax liability
10 actually was, given the constraints that we were facing in
11 terms of the -- of what the documentation the United
12 States has versus what documentation we might receive from
13 the Republic of Iran.

14 JUDGE VASSIGH: This is Judge Vassigh. Thank
15 you.

16 I'd like to check in whether -- Judge Tay, do you
17 have any questions for either of the parties?

18 JUDGE TAY: I just have one question for
19 Franchise Tax Board. Would you like to respond to the
20 reasonable cause argument for the accuracy-related
21 penalty?

22 MR. HUNTER: Yes, I would. I pass that one over
23 to my colleague, Ms. Monet.

24 MS. MONET: Hi. Thank you. This is Marguerite
25 Monet. You know, I think the problem here -- and I think

1 that the standard of the defense for reasonable cause and
2 good faith is essentially what the taxpayer -- what the
3 Appellants have described. I think, you know, what we
4 lack here is facts about the Appellant's efforts to
5 determine whether they could take this loss, the treatment
6 of the item, in the tax year in question, and you have to
7 look at the time they filed the return. And I think in
8 that regard, Panel, that the Appellants have not detailed
9 what they did.

10 Did they discuss it with a tax adviser? Did they
11 consider at that time? Did they consider cases that
12 interpreted an expropriation loss and its ability to be
13 deducted and what year it should be deducted? Did they
14 consider evidentiary problems they might have with the
15 documents in question? So I think simply it's not that
16 they didn't state what that defense is correctly. I think
17 they simply haven't established the elements of that
18 defense.

19 Thank you.

20 JUDGE VASSIGH: Thank you.

21 I'd like to see if Judge Lambert has any
22 questions for either party.

23 JUDGE LAMBERT: This is Judge Lambert. I don't
24 know if this was addressed before. But, Appellants, can
25 you address FTB's argument that the appraisal, you know,

1 has no comparables, and it kind of just declares the
2 value, it seems, without any appraisal method,
3 necessarily, that -- like, a comparable property method.

4 MR. CORBIN: Well, I think the individual that
5 was hired was a professional individual to provide an
6 appraisal relative to a property within the Iranian
7 country. And so we had some challenges in that they could
8 just throw out a number, and it might not necessarily be a
9 true number. And so the methodologies employed with the
10 valuation aspect were not necessarily ones that we would
11 recognize from a U.S. perspective. They were relevant
12 from an Iranian perspective and with Iranian
13 professionals.

14 So from our perspective, when it comes to
15 evaluation, we did our due diligence in hiring the
16 relevant individuals understanding that they may not have
17 been the exact same as U.S. persons. But they were
18 relevant to the fact that we cannot get access to the
19 property because of the revolution and that they might
20 have a methodology different from the United States. And
21 so we had to go through that, translating it into an
22 actual U.S. dollar number and providing documentation to
23 the Franchise Tax Board.

24 JUDGE LAMBERT: This is Judge Lambert. Thank
25 you. And no further questions.

1 JUDGE VASSIGH: Thank you, Judge Lambert. I'd
2 like to go back to Judge Tay who indicated he had another
3 question.

4 JUDGE TAY: Yes. Thank you, Judge Vassigh.

5 Question for Appellant. Would you like to
6 respond Mr. Hunter's analyses of the cases you provided
7 today in regards to the holding the property for a profit
8 motive or in a trade or business?

9 MR. CORBIN: Well, I think that when you look at
10 Mr. Babaoff and his father when they removed themselves
11 from Iranian conflict, they came here with a distinctive
12 purpose to generate income and develop property. That
13 would indicate that everything that they would do relative
14 to any property holdings would be for the indication of
15 business purpose.

16 The case law that Mr. Blau has indicated was a
17 high-level indication that would correspond to what
18 Mr. Babaoff's approach was to any property ownership. And
19 if you look at the history from when he came here to the
20 United State and his tax returns, you can see that there
21 is a material amount. In fact, that's all he does is to
22 develop property.

23 And so by the ownership of the property in Iran
24 up until it was fully executed and taken by the Iranian
25 government, his whole indication was to ultimately move

1 back to Iran and develop the property and sell it for a
2 profit, which would meet the motivation and for-profit and
3 allow ability for the deduction.

4 JUDGE TAY: Thank you. One more question for
5 Appellant. Mr. Babaoff, testified to the fact the
6 government had come in prior to 2011 with the intention to
7 confiscate the property. And so one question that I have
8 is when would you say he was deprived of all benefit of
9 the land? If the process had begun in 2008 or 2009 and it
10 was basically just a matter of time, then why shouldn't we
11 consider 2008 or 2009 to be the actual date of
12 confiscation?

13 MR. BABAOFF: Do you want me to respond to that?

14 MR. CORBIN: Yes, you can. Please respond to
15 that.

16 MR. BABAOFF: The instigation for when the
17 process started was when my uncle went to try to sell the
18 property. At the time, they said okay. You're not
19 allowed what they call -- they put a hold, a lien. It's
20 not a lien really. It's a hold on the title, basically
21 saying this property is not to be sold. And at the time,
22 basically, we still own the property, and they go through
23 a -- sort of a legal process to confiscate the property.
24 And that took up to two years to finally confiscate it,
25 and we got the Notice of Confiscation.

1 MR. CORBIN: And, Kam, I have some questions for
2 you. My understanding is there had been a correspondence
3 that was actually threatening and allow you to stop the
4 process, so to say, in 2011. In other words, the finality
5 of the absconding of the property was not only related to
6 the legal process in Iran but also a personal threat, is
7 my understanding.

8 MR. BABAOFF: Correct.

9 JUDGE TAY: Thank you. I have no further
10 questions.

11 JUDGE VASSIGH: This is Judge Vassigh. Does
12 anyone else have any questions?

13 Okay. We are ready to conclude this hearing.
14 The record is now closed.

15 Thank you everyone for coming in today.

16 And thank you Mr. Babaoff for your testimony.

17 I'd like to thank Ms. Alonzo and OTA staff who
18 are working behind the scenes for us to hold this
19 electronic hearing.

20 This matter is now submitted to the panel to
21 privately confer and decide the issues. We will aim to
22 send you a written opinion of our decision within 100 days
23 from today.

24 Today's hearing in the Appeal of Babaoff is now
25 adjourned.

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25

Thank you again everyone for your presentations.
We will now adjourn for today.

(Proceedings adjourned at 3:38 p.m.)

~0~

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25

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 21st day of February, 2022.

ERNALYN M. ALONZO
HEARING REPORTER