OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

In the Matter of the Appeal of: **B. FOGEL AND** **R. FOGEL**	OTA Case Number 20025864

OPINION

Representing the Parties:

For Appellants: Dennis L. Perez, Attorney

For Respondent: Bradley J. Coutinho, Tax Counsel III

For Office of Tax Appeals: Tom Hudson, Tax Counsel III

T. STANLEY, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19045, B. Fogel (appellant-husband) and R. Fogel (collectively, appellants) appeal from the action of respondent Franchise Tax Board (FTB) in proposing to assess additional tax of $372,442.00, a post-amnesty penalty of $18,053.03, and applicable interest for the 2002 taxable year.

Appellants waived their right to an oral hearing, so the Office of Tax Appeals (OTA) decides the matter based on the written record.

ISSUES

1. Is the proposed assessment barred by the statute of limitations?
2. Have appellants shown error in the proposed assessment?
3. Does OTA have jurisdiction to abate the post-amnesty penalty?

FACTUAL FINDINGS

1. Appellants filed a California income tax return for the 2002 taxable year reporting total tax of $69,517.[1]

[1] The tax return itself has not been provided for this appeal, but FTB submitted a screenshot showing "Taxpayer Data" from appellants' 2002 tax return. Appellants do not dispute this return information.

2. Appellants each owned 50 percent of Western Medical Group, LLC, a pass-through entity. Appellant-husband signed a plea agreement with the U.S. Attorney's Office and U.S. Department of Justice, Tax Division on December 4, 2014 (Plea Agreement). As relevant here, Attachment A to the Plea Agreement states that appellant-husband used various foreign bank accounts as part of a complicated scheme (or "plan") to claim a $4,000,000 false business expense deduction for Western Medical Group, LLC in 2002. The Plea Agreement states that, "The false expenses were characterized as, among other things, 'Outside Services' and 'Information and Services Tech' on Western Medical Groups [*sic*], LLC's 2002 tax return." The Plea Agreement further states that appellant-husband knew no services were provided for the purported expenses and that "the deductions suggested by [D. Kalai,[2]] were false and were used to falsely reduce the amount of tax owed by [appellant-husband.]"[3]
3. On July 13, 2017, FTB issued a Notice of Proposed Assessment (NPA) to appellants based on the Plea Agreement, proposing to increase appellants' taxable income by $4,000,000 and reducing appellants' deductions by $4,776 due to the phase out of itemized deductions. FTB proposed to assess additional tax of $372,442.00 and a post-amnesty penalty of $18,053.03, plus applicable interest.
4. Appellants protested the NPA, and FTB issued a Notice of Action, affirming the NPA. This timely appeal followed.
5. On appeal, appellants acknowledge that their business objectives did not require offshore banking.
6. On September 14, 2020, during the pendency of this appeal, the IRS assessed additional federal tax with respect to appellants' 2002 federal tax account.

[2] According to the Plea Agreement, appellant-husband retained D. Kalai to prepare his individual tax return and the corporate tax returns related to appellant-husband's medical practice, and later to prepare tax returns for his managed healthcare business entities.

[3] The details of the plan set forth in the federal Plea Agreement are beyond the scope of this decision. The key fact is that as part of his federal Plea Agreement, appellant-husband acknowledges claiming a $4,000,000 false tax deduction in 2002, knowing he was not entitled to it.

DISCUSSION

Issue 1: Is the proposed assessment barred by the statute of limitations?

Generally, FTB must issue a proposed assessment within four years of the date the taxpayer filed his or her California tax return. (R&TC, § 19057(a).) However, R&TC section 19087(a) provides that FTB may propose to assess the amount of tax, interest, and penalties due "at any time" when a taxpayer files a false or fraudulent tax return with the intent to evade the tax. A tax return that is filed with the government (here FTB) with the taxpayer's knowledge of its falseness is intended to deceive and defraud the government. (*Emmich v. U.S.* (6th Cir. 1924) 298 F.5, 10, cert. denied 266 U.S. 608.)

The Plea Agreement states that appellant-husband used various foreign bank accounts to claim a $4,000,000 false business expense deduction for Western Medical Group, LLC, which flowed through to appellants' individual tax return. Furthermore, appellants acknowledged that their business objectives did not require offshore banking. The record reflects that appellant-husband was a sophisticated businessperson who admits he falsified his tax returns by claiming a false business deduction. Although the fraudulent scheme was proposed by D. Kalai, appellants' tax advisor at that time, appellants followed the scheme and took the steps that created the false deduction with an intent to evade tax when appellants filed their 2002 tax return.

Appellant-husband knew no services were provided for the purported expenses and that "the deductions suggested by [D. Kalai] were false and were used to falsely reduce the amount of tax owed by [appellant-husband]." Thus, appellants filed a false return and pursuant to R&TC section 19087, FTB's proposed assessment may be made "at any time."

On appeal, appellants also assert that the $4,000,000 payment was paid to compensate appellant-husband's sister for services she performed for appellants' businesses. However, appellants have not presented evidence showing what services were performed, whether appellant-husband's sister was ever paid, or why appellant-husband signed the Plea Agreement admitting to taking a false business deduction if appellants' claims are true. Unsupported assertions are insufficient to carry appellants' burden to show error in FTB's proposed assessment. (*Appeal of Vardell*, 2020-OTA-190P.)

Issue 2: Have appellants shown error in the proposed assessment?

FTB's determinations are generally presumed correct, and the taxpayer bears the burden of proving otherwise. (*Appeal of Vardell*, *supra*.) Income tax deductions are a matter of legislative grace, and a taxpayer who claims a deduction has the burden of proving by competent evidence that he or she is entitled to that deduction or credit. (*Ibid*.) Unsupported assertions cannot satisfy a taxpayer's burden of proof. (*Ibid*.)

Appellants assert that appellant-husband's plea referred only to his failure to file certain required forms related to ownership of foreign bank accounts. Appellants also contend that the other statements in the Plea Agreement were included because the federal government wanted to build its case against D. Kalai. Appellants urge OTA to conclude that those statements attributed to appellant-husband should not be considered factual admissions by appellant-husband.

Appellants do not deny taking the deduction on both their federal and California returns for 2002. It is appellants' burden to prove that they were entitled to the $4,000,000 business deduction. Appellant-husband, in the Plea Agreement, admitted that appellants falsely claimed a business expense deduction of $4,000,000 for the pass-through entity known as Western Medical Group, LLC. Appellant-husband approved and signed the Plea Agreement, which is an official government document filed with the U.S. District Court for the Central District of California. The acknowledgements of wrongdoing in the Plea Agreement do not support appellants assertion that the deduction was a proper one to pay appellant-husband's sister for services she rendered.

Appellants acknowledged that their business objectives did not require offshore banking, but they assert they were "naive" and relied on D. Kalai's advice to engage in the illegal scheme described in the Plea Agreement. D. Kalai's specific advice is not included in the record for this appeal, but the available evidence does nothing to show error in FTB's determination. Despite appellants' assertions suggesting appellant-husband was somehow coerced by the federal government to admit to creating a false tax deduction, appellant-husband signed documents in which he unequivocally stated that the foreign bank account scheme or plan created a false business deduction with the intent to evade tax. Appellants have not supported their assertions with any evidence to contradict the statements in the Plea Agreement. Consequently, appellants have not met their burden to show error in the proposed assessment, which OTA sustains.

Issue 3: Does OTA have jurisdiction to abate the post-amnesty penalty?

R&TC sections 19730 through 19738 set forth the tax amnesty program. During the amnesty period, which ended on March 31, 2005, the tax amnesty program applied to tax liabilities for taxable years beginning before January 1, 2003. (R&TC, § 19731.) R&TC section 19777.5(a)(2) provides that a penalty shall be added to the tax for each taxable year for which amnesty could have been requested for amounts that become due and payable after the last day of the amnesty period. The penalty amount is equal to 50 percent of the interest on any final amount for the period beginning on the last day prescribed for payment of the tax (here April 15, 2003) and ending on the last day of the amnesty period (March 31, 2005). (*Ibid*.) For amounts assessed after the last date of the amnesty period, the related penalty is commonly referred to as the post-amnesty penalty.

FTB has no discretion to determine whether the post-amnesty penalty should be imposed, and there are no statutory exceptions for taxpayers who may have acted in good faith, reasonably relied on advice of a professional, or had reasonable cause for failing to participate in the amnesty program. Review by OTA of FTB's imposition of the post-amnesty penalty is strictly limited. The only situation that would allow OTA to review a post-amnesty penalty assessment is when the denial of a taxpayer's claim for refund was filed on the basis that FTB erred in its computation of the penalty. (R&TC, § 19777.5(e).) Appellants have not asserted or shown that they paid the penalty nor that it was incorrectly calculated. Under these circumstances, OTA lacks jurisdiction to consider the post-amnesty penalty.

HOLDINGS

1. The proposed assessment is not barred by the statute of limitations.
2. Appellants have not shown any error in the proposed assessment.
3. OTA does not have jurisdiction to abate the post-amnesty penalty.

DISPOSITION

FTB's proposed assessment is sustained.

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Teresa A. Stanley
Administrative Law Judge

We concur:

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Richard Tay
Administrative Law Judge

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Veronica I. Long
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Veronica I. Long
Administrative Law Judge

Date Issued: 4/20/2023