BEFORE THE OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

IN THE MATTER OF THE APPEAL OF,	
M. SEGAL and A. SEGAL,	OTA NO. 21067917
APPELLANT.	

TRANSCRIPT OF PROCEEDINGS

Cerritos, California

Tuesday, September 12, 2023

Reported by:
ERNALYN M. ALONZO
HEARING REPORTER

BEFORE THE OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

IN THE MATTER OF THE APPEAL OF, M. SEGAL and A. SEGAL, APPELLANT.	OTA NO. 21067917

Transcript of Proceedings, taken at 12900 Park Plaza Dr., Cerritos, California, 91401, commencing at 9:41 a.m. and concluding at 11:00 a.m. on Tuesday, September 12, 2023, reported by Ernalyn M. Alonzo, Hearing Reporter, in and for the State of California.

APPEARANCES:

Panel Lead:	ALJ ANDREA LONG
Panel Members:	ALJ AMANDA VASSIGH ALJ SHERIENE RIDENOUR
For the Appellant:	WILLIAM WEINTRAUB
For the Respondent:	STATE OF CALIFORNIA FRANCHISE TAX BOARD DAVID HUNTER

I N D E X

E X H I B I T S

(Appellant's Exhibits 1-8 were received at page 6.)

(Department's Exhibits A-V were received at 6.)

OPENING STATEMENT

WITNESS TESTIMONY

PRESENTATION

CLOSING STATEMENT

Cerritos, California; Tuesday, September 12, 2023

9:41 a.m.

JUDGE LONG: We are ready to go on the record.

Welcome to the Office of Tax Appeals. This hearing is taking place in Cerritos, California. Today is Tuesday, September 12th. It is 9:41 a.m. This is for the Appeal of Segal. The Case Number is 21067917.

We will begin with the parties introducing themselves. Let's start with FTB.

MR. HUNTER: Good morning. David Hunter, H-u-n-t-e-r, on behalf of Respondent Franchise Tax Board.

JUDGE LONG: Thank you.

Appellants.

MR. WEINTRAUB: William Weintraub on behalf of Appellants Mark and Arlene Segal.

JUDGE LONG: And with you I see Mr. Segal; is that correct?

MR. SEGAL: Yes.

JUDGE LONG: Thank you.

So the issue that we are discussing today is whether Appellants have established error in FTB's disallowance of Appellants' claimed bad debt deduction for 2013.

Appellants submitted Exhibits 1 through 8, and

it's hereby admitted without objection.

(Appellant's Exhibits 1-8 were received in evidence by the Administrative Law Judge.)

JUDGE LONG: FTB submitted Exhibits A through V, and it's admitted without objection.

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

JUDGE LONG: And the parties have indicated before we went on the record that they have no additional exhibits to submit. So I believe we are ready to begin.

We will begin with Appellants' opening statements.

Mr. Weintraub, you have 10 minutes for your statement. You may begin.

MR. WEINTRAUB: And thank you, Judges.

OPENING STATEMENT

MR. WEINTRAUB: The issue as you correctly stated is the deductibility of a bad debt loss in 2013. The loss arose on a tax year return 2012. It was not used in 2012 and was carried over to 2013. The year of audit was 2013 because the 2012 year was closed by the statute of limitations. So at the outset we have a loss carried over from a closed year.

With respect to the tax issues related to the

deductibility of the loss, there are essentially three that have been addressed in the briefs. First was the amount of funds provided by Mr. Segal to Mr. Roberts, a loan -- a bona fide loan. The FTB has contended that it was not a bona fide loan for the reasons that we'll -- I'll go through in my arguments. We believe that it's clearly a bona fide loan.

The second issue that comes up is a portion of the funds that Mr. Segal provided on behalf of Mr. Roberts, was the payoff directly to third parties for who -- one case, Mr. Segal entered into a written guarantee, and another case, it's simply paid off the debt that Mr. Roberts owed to a third party thereby, adding that amount to what was owed by Mr. Roberts to Mr. Segal. So the question has arisen as a legal matter. Is this deductible as a bad debt? And one in particular, which was covered by a written guarantee, was that guarantee properly deductible as a bad debt.

The final issue that we will address is the proper year for the deductibility. Mr. Roberts had been borrowing money from Mr. Segal over a -- many, many years going back to the early 1980s and have been repaying those loans over the years. Mr. Segal, on account of his long history of dealing with Mr. Roberts, expected repayment of all amounts until the year in which he finally deducted

the loss, which was 2012.

The FTB has asserted that 2010 was the proper year for the bad debt deduction which, unfortunately, for the Segals is a closed year. The reason the 2010 was asserted was Mr. Roberts major asset, which was his residence, a various substantial ranch, was lost in a foreclosure proceeding. But that wasn't the end of Mr. Roberts' ability to repay. Mr. Segal being a sophisticated tax accountant understood the rules that you can't simply deduct a loss because of a bad -- one bad event. You have to establish that there's no prospect of recovery.

And based upon the long history of working together, Mr. Roberts' other assets, which were known to Mr. Segal, and his communications with Mr. Roberts, he was led to believe, and had good reason to believe, that the loan would still be repaid. And although it would have benefited him to claim the deduction earlier in 2012, he did not do so. He waited until -- I'm sorry. It would have benefited him to deduct the loss in 2010. He waited until 2012 when it was absolutely certain that there was no prospect for repayment. So as to the timing, we believe the 2012 was the correct year.

I have no further statements for the opening.

JUDGE LONG: Thank you.

Mr. Hunt, you may begin your opening statement.

OPENING STATEMENT

MR. HUNTER: Thank you. Again, David Hunter on behalf of Respondent.

This case involves a disallowed non-business bad debt deduction. The facts and evidence will show that Appellant is not entitled to a $2 million bad debt deduction, which was reported as a short term capital loss. Appellant took upon himself to get involved with an existing lender debtor relationship that went array. When his management firm advised clients to make a loan that was subsequently not being repaid, the Appellant pulled out his personal checkbook and performed damage control. But when he personally guaranteed the debt of another, because the loan had gone bad, he took a risk.

And our presentation will match the flow of Appellants' presentation. Because under these facts, this effort does not give rise to a bad debt deduction. He provided -- Appellant provided no evidence that he entered into these guarantees for profit and that he received reasonable consideration in return. Appellant also provided cash directly to the debtor. Appellant said he used to personally loan this debtor money throughout the years.

However, these cash outlays that are at issue in this case do not rise to the level of being a bona fide debt that gives Appellant a bad debt deduction on his tax return, his personal tax return. There was no possibility of repayment when Appellant made these cash outlays to Appellant -- I'm sorry -- to the debtor. Sorry about that.

Finally, it is apparent from an objective standpoint that the debtor had no ability to repay any loans as of 2010, and this case deals with a deduction that was reported in 2012 but taken in 2013. That's the tax effect, and that is the assessment that was imposed. The law is clear. Upon examination by Respondent, Appellant must show he falls squarely within the perimeters of the deduction as provided by the legislature. He did not do so in this case, and Respondent's action in disallowing these bad debt deductions should be sustained.

Thank you.

JUDGE LONG: Thank you.

So we will move on to Mr. Segal's testimony.

Mr. Segal, I'm going to swear you in now. If you can raise your right hand.

///

///

M. SEGAL,

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

JUDGE LONG: Thank you. You may begin.

WITNESS TESTIMONY

MR. SEGAL: Thank you.

I have some prepared comment statements that will help you better understand context. What you've heard so far has zero context. So I'm going to give you some context.

In 1981, two partners and I left a Big 8 accounting firm and started our own practice. This practice was in a unique environment. Today if you live in LA or New York you understand when people refer to people as business managers. You might better understand who we are as personal CFOs providing unlimited concierge-related services to high-net-worth individuals. Best way to explain it to you and is easy to understand. Anything you ever in your life pick up a phone and call something to do, we do.

So in 1981, when he started business, there was three of us. Today we are the largest firm of this kind

in America. There are 670 employees and 54 partners. Help a little more just in context of who we were and who we represent, today if you looked at the last 15 Super Bowls, our clients did the halftime show 13 times. Again, for context.

So when we started the business in 1981, you can imagine three of us and an assistant. There weren't a boatload of clients. Ken Roberts was referred to us four or five months after we started business. To this day it is the most unique referral I've ever had since I've been in business. He was referred to us because in Mandeville Canyon -- if you know Southern California, this is a canyon on the west side of town up in the mountains above Pacific Palisades.

There was a flood. He had a property worth tens of millions of dollars, a home, et cetera. The home was completely destroyed. And the only reason he is alive, he had a dog doing back flips in a doorway to get his attention and wouldn't stop barking. He ran and grabbed the dog and the back wall fell in as the mud came through. So he came to us and said look, "I have no books and records. I need to reconstruct my life. Will you guys help me do it?"

So we -- we were young. We were very good accountants, and so we said sure. And so what happened is

in December of 1981 he came into the office one day, and for the next 11 months, five days a week 9:00 to 6:00, he was in a conference room with one of my senior employees reconstructing his books and records. When we got done, he didn't have a lot, except a piece of property. He went out and what he decided he was going to do is the radio station -- if you live down here, you would know it's called KROQ, K-R-O-Q -- was not on air.

He actually went, settled with all of the vendors and put the station back on air. That was in '82 or '83. And in '84 or '85 he sold it for $60 million, I believe. His main way of making revenue was in the market. He was an investor in the stock market. Took those monies, put it in the mark, and we all know what happened in 1987. The market crashed. 100 percent margined. Broke again.

So during these time periods, early in '82 he came to me and said, "Would you consider lending me some money, and I will pay you back in the following way. I will give you a stack of post-dated checks for interest and stack of principal repayments and you can deposit them on that date."

I was the only one doing it. I did it. I did it two or three different times for different amounts. Never missed a payment. Never had a bounced check, and never had a problem. So as time went on his need got greater

and a few other people did it. Same problem -- same issue. Never default. Never a missed interest payment. Never a bad check.

So finally a client of mine knew him and asked about this. And told him yes, I'd been doing it. And this client says well, I'm going to do it. He is as good as gold and there's no chance you won't repay. So that client did it. So over the next 20 years Ken was probably lent in the vicinity of $10 million of which he repaid every dollar and every dollar of interest to every person who lent it to him.

After '87 he had to start over. He had an ingenious idea. To this day I'm not sure it's been done again. He took an FM station and an AM station with the same call numbers and by technology joined them into one station and covered two communities in Southern California. In the late -- middle to late 90s he sold that for $80 million. Of course, back into the market and 2000 tech boom crash, 911 and the aftermath. Basically, broke again.

So all during these periods he was borrowing money because he was making money at a far higher rate then he was paying interest. So there were some existing loans and some new loans that were made. He had already come from nothing to something three times. It certainly

isn't a natural conclusion it will never happen. He clearly proved that it can happen again. So he worked on a lot of different things during this time period. During this time period a couple of clients who had lent to him multiple times -- we're not talking three or four times, six to seven times, eight times -- lent money to him. Some larger denominations.

As we went there you the 2000 through 2010 period these notes -- big notes started to come due. He couldn't repay them at the time they came due. So I'm sitting on a business that's 100 percent reputation driven. If I don't satisfy those loans, the damage to the reputation to the business could have been catastrophic. Two phone calls to a Daily Variety or a Hollywood reporter or today there's the equivalent of the Daily News and your story would be all over the street. I lent this money to a client. My accountant thought it was a great idea. I had been repaid eight times. This time I didn't. It would have been a destructive process.

And so I repaid those clients. You could argue I lent him the money and he repaid them. The checks came directly from me to that client, and I repaid those clients. And I repaid them because of the business risk. And in looking back at this in hindsight, there's a legitimate argument. It was an ordinary deduction as

opposed to a capital loss.

It was clearly a business deduction because it could have destroyed the business. Ad so preservation of that business would make it a business -- you know, a business deduction related to the extent of taking it in that basis, which we didn't do. Now, we got into the later 2000s, and in 2009 and 2010 they foreclose on his house. He has three different deals that he's working on. If any one of the three happen, in the worse case he gets $75 million. You could argue he has no assets, but had no assets three times before and built assets. And these are all, by the way, traceable events because the sales were public, meaning they received press, et cetera, et cetera, when he sold these radio stations.

So there certainly wasn't anything in 2010 that said to us, me personally, that I won't get repaid. I spoke to this client three or four times a month for 30 years. I trusted this client, even though I was forced to do something to protect our own reputation. I trusted this client, and I believe I'd get repaid. And there was never an incident where I hadn't gotten repaid, even in a case like this.

Then in 2012 he became sick. It became clear he wasn't going to be able to continue to work, and he passed shortly thereafter. And that's where we ended up taking

our business bad debt -- excuse me -- our bad debt loss. And for what it's worth, I had a partner by the name of Fred Nigro who was audited by the FTB with the exact same facts that I have to the extent lending money to this client. That audit resulted in no change, and he took a bad debt loss at the same time.

So I think I've covered most of the facts in a background for you to understand. It isn't some fly by night lender deal. This client was a client of mine for 33 years. When I got him he didn't have $0.04. I watched him make $60, $70 million. I watched him lose $60, $70 million. I watched him make $80 or $90 million, $100 million. I watched him lose a $100 million. Along the way clients, friends of his, myself, some of my partners lent him money all along the way. There was never a non-repayment.

As times got more difficult for him, late in the 2007, '08, '09, '10 period it became harder. The small amounts got repaid. These two big loans became a problem. I couldn't afford to take the business risk that it could have resulted in, and so I repaid those client. It wouldn't have been any different if I lent him the money, he repaid them, and I had a bad debt. The results are exactly the same. It wouldn't have been repaid.

So I think that covers all the facts, and I'm

happy to answer any questions.

JUDGE LONG: Thank you.

Mr. Hunter, do you have any questions?

MR. HUNTER: No.

Mr. Segal, I thank you for that testimony. I have no questions.

JUDGE LONG: Okay. I'm going to turn it over to my Panel members. On the panel with me are Sheriene Ridenour and Amanda Vassigh.

Judge Vassigh, do you have any questions.

JUDGE VASSIGH: I do.

Just a quick point of clarification. I believe that in your opening brief you stated that the bad debts claimed in 2012 were non-business bad debts. Can you clarify your position on whether they were non-business bad debts or not?

MR. WEINTRAUB: They were claimed as non-business bad debts, which provides a short-term capital loss treatment, which is not the best. What Mr. Segal described is, the payment of an obligation in a trade or business would give rise to an ordinary loss to the payment to protect a business reputation could have given rise to an ordinary loss, but that's not the position taken on the return. The position was non-business capital loss treatment, which as a result there weren't

sufficient capital gains in 2012. So the unused loss carried over to 2013.

JUDGE VASSIGH: Thank you very much.

JUDGE LONG: Judge Ridenour, do you have any questions?

JUDGE RIDENOUR: None at this time. Thank you.

JUDGE LONG: All right. Thank you.

We can move onto Appellant's arguments. You may begin when you're ready.

PRESENTATION

MR. WEINTRAUB: Okay. The arguments with respect to the bad debt are number one, was this bona fide debt. And the FTB has asserted it was not a bona fide debt. And I would ask the question: What else could it have been? There was nothing else that it could have been but a loan. So the FTB's argument that this was not a bona fide loan, there is no other explanation for what it could be. Every single case that's reported dealing with the issue of whether a transaction is a bona fide debt looks at it to say it's not a bona fide debt because it's something else.

It's an equity contradiction. It's a capital, it's a gift. There is no other possible characterization of what -- of how you would treat the funds that Mr. Segal provided to Mr. Roberts. It's not enough to say well, it

was not a debt. Well, if it wasn't a debt, if it wasn't a bona fide loan, please tell me what else it was. Because it -- but I believe there is no other characterization.

Secondly, there were promissory notes for each of the loans. There was documentation. Was it the same formal loan documentation that if you got a mortgage on your home and you have a stack of papers three-inch thick? No. But that's not required. There was clear evidence that this was intended by both Mr. Segal and Mr. Roberts as loans. They documented it that way. They both treated it that way. There was a long history, a very long history, as Mr. Segal has testified, of loans made to Mr. Roberts and loans repaid.

So given that there's nothing else it could be, given their long history of working together, given the documentation that existed, I again ask the question, what else could it be if it's not a loan? So we believe that the evidence clearly establishes that these were bona fide loans. The briefs provide the legal analysis of the case law that supports that. But in every one of the cases -- you could read a thousand cases on whether something is bona fide debt -- and in almost every one of them, if a court said it's not bona fide debt, they said well, it's because it's something else.

It was really equity. It was really a loan. It

was something else. But there is nothing else that we could characterize this as other than a loan between Mr. Segal and Mr. Roberts. So we believe that the facts and the law clearly support that these were bona fide debts. And, unfortunately, if you read the briefs back and forth between Appellants and the FTB, there's a lot of back and forth on this. So it's all in the briefs. But it's the same arguments I've made throughout the briefs. There is nothing else that this could have been.

Now let's get to the issue of where the guarantees come in. So to break it down of the loans that are in issue, there were five amounts that were loaned directly to Mr. Roberts totaling a little over $500,000. There were two other amounts where Mr. Segal provided funds on behalf of Mr. Roberts. One was a payment pursuant to a written guarantee on a loan to Roseanne Bar where Mr. Roberts did not pay. The second was a payment to Ben Thomas on loans that Mr. Thomas had made to Mr. Roberts that had not been repaid.

As Mr. Segal has testified, these people made their loans to Mr. Roberts based upon his say so. They relied upon Mr. Segal for everything that they did financially. He said make the loan. If he says the loan is good. They believed him. They trusted him. They made it. Now you could say they are adults. They should bear

the risk if Mr. Roberts doesn't pay, but that's not the way it works, particularly, in this city, in the entertainment industry.

Had they not been repaid, as Mr. Segal has testified, the consequences to his practice, the consequences to his firm, would have been devastating. He was forced. He didn't do this out of charity. He wasn't making a gift to Mr. Roberts. There's no other reason that he would have paid these loans, paid on the guarantee -- the written guarantee on the Roseanne Bar loan and the oral arrangement with Ben Thomas for a million dollars. Why would he do this? Was he making a gift?

Mr. Roberts wasn't his child. This was not part of an estate plan to transfer wealth. This wasn't giving Mr. Segal an ownership interest in anything that Mr. Roberts had. There was no equity contributions. There was no capital, no asset that he acquired as a result of making this other than a receivable from Mr. Roberts. So the fact that it was not paid directly to Mr. Roberts, he made a payment on his behalf, and that's a loan.

Now as to the payment on the Roseanne Bar, that was a payment of a guarantee. And there it gets a little bit more complicated because if you look at the

regulations on paying a guarantee, the regulations were concerned that a parent might guarantee a loan for a child. And if they pay it off, they're really making a gift to a child. That wasn't the case here.

So the regulations say if you're making a payment as a guarantor and you're out the money, it has to be something that's not a gift. There has to be some profit motive or some other indirect benefit to you. And as I have gone through it and as Mr. Segal testified, the indirect benefit was the protection of his reputation, the protection of his trade or business, the protection of his business management firm, which by the time he made these payments was very substantial. So he really had no choice. There was the benefit, which was the protection of the reputation, the protection of the business.

So even if viewed in the guarantor context, it would be properly treated as a bad debt. But you could look at it as a payment or a guarantee or you could simply look at it as an additional loan made by Mr. Segal to Mr. Roberts. Again, the payments don't have to go directly to him to qualify as a loan if he pays something on behalf of Mr. Roberts that too is a loan. So the million dollars loss that was claimed on repaying the loan made by Ben Thomas, the $600,000 loss claimed on the loan made to Roseanne Bar, those were bad debts for Mr. Segal.

Whether run them through the guarantee analysis or just through the plain bad debt analysis.

Then we get to the issue of well, why didn't he deduct them earlier. The FTB argues that when he made loans, when he made the payments, he had no prospect of repayment. And therefore, that's why number one, they weren't bona fide loans. And number two, if they were, they should have been claimed as losses in 2012. Well again, for the reasons that Mr. Segal testified, he had every reason to believe all along that he would be repaid based upon the long 20-plus year history with Mr. Roberts borrowing, repaying, borrowing, repaying, occasionally having a massive transaction resulting in a substantial gain.

And it would have benefited Mr. Segal to claim a deduction much earlier. Why not? You have a reduction in tax earlier. Why would you wait to do it? Mr. Segal waited because he understood the rules. You cannot claim a deduction on a bad debt until it's worthless. In 2010 it was not worthless. He had been in regular contact with Mr. Roberts. Mr. Roberts assured him that he was working on things that would result in repayments, and Mr. Segal credibly believed that.

Now, if you want to say that was not credible to believe that, then you have to disregard the 20 years when

Mr. Roberts did come through and make the repayments, and disregard the fact that it would have been in Mr. Segal's interest to simply say fine, I'll deduct it in 2010. But for the history and Mr. Roberts' assurance, Mr. Segal was willing to wait a little longer to see if there was any prospect for any repayment.

And finally after Mr. Roberts became ill in 2011 and very ill in 2012 and as much has conceded that he had no ability to repay. That finally became the proper year for the deduction. Mr. Segal tried to turn square corners, tried to do it right. Not try to be greedy about it. Not to be cute to say well, the fact that he lost his house that's a good reason. I'll claim the bad debt deduction now. He waited until he was absolutely certain that there was no prospect for repayment. And when he claimed the deduction as the tax preparer for Mr. Roberts, he also had to report that the relief of the bad debt resulted in a loss of tax attributes for Mr. Roberts.

A cancellation of debt because Mr. Segal claimed a bad debt on Mr. Roberts' side, the relief of bad debt is income. And since he did not have income, the effect of the relief of the bad debt is to reduce tax attributes. So Mr. Roberts had a loss carryover, some other tax attribute, the cancellation of debt which was not taxable to him because of its insolvency, resulted in the loss of

his tax attributes.

And that was reported that way on Mr. Roberts' tax return. There was a form that was filed, and it's one of the exhibits, to show that Mr. Roberts reported this as cancellation of debt. He concurred that this was the proper year and he, at that point, surrendered whatever tax benefits he would have had that still remained. He gave them up. If it was a net loss carryover, that carryover would have been reduced dollar for dollar by the bad debt that he did not have to report because he was insolvent. So it's fairly clear that there was no choice for Mr. Segal other than to wait until there was no prospect.

You can't say it was partially worthless. The rules don't work that way for deducting bad debt. You can't say I think I can only collect 50 percent of my loan. I can only collect 30 percent. You have to wait until there's no reasonable prospect of recovery. And in 2010, I think it's very credible that Mr. Segal believed that there was a prospect of recovery. By 2012, given what had happened for a number of years and in particular given the fact that Mr. Roberts became severely ill and could no longer work on the types of transactions that resulted in repayment, Mr. Segal determined that would be the proper year to claim the deduction and did so.

So for all of the reasons we think this was a bona fide debt, the loans that were made to Mr. Roberts by Mr. Segal were made with the expectation of repayment. When the loans went to Mr. Roberts they were evidenced by promissory notes. When payments were made to third parties, they were acknowledged as additional advances to Mr. Roberts. There should be no dispute that these were nothing other than loans. And I would love to hear some explanation that the money transferred from Mr. Segal to Mr. Roberts was something other than a loan.

And so for these reasons we think that the loss was properly claimed on the 2012 return, which is closed, which raises an interesting issue. The FTB missed the opportunity to challenge in 2012 whether these were bona fide loans, to challenge in 2012 whether that was the proper year to deduct the loss. It didn't occur. And if Mr. Segal had the income in 2012 to offset -- to be offset by the losses, he would have used them in the year. There would be no carryover, and we wouldn't be sitting here today.

But he didn't have sufficient capital losses to use. I'm sorry. He didn't have sufficient capital gains to use the losses because non-business bad debts can only be deducted against other capital gains or they are limited to $3,000 against other income. Mr. Segal did not

have substantial capital gains in 2012. Therefore, the capital losses he reported and deducted carried over to 2013, which is the year that's before you now.

But absent a disallowance of the deduction in 2012, it's hard for me to understand how the FTB can now say that these were not bona fide loans, how they can say 2012 wasn't the proper year. There was an opportunity, but they didn't do it. And since the year is closed, I think those issues should be off the table for consideration.

And so in conclusion, I think the returns were properly filed. I think that Mr. Segal should be entitled to the deduction and should not have any deficiency as claimed by the FTB.

JUDGE LONG: Thank you, Mr. Weintraub.

Mr. Hunter, you have 20 minutes for FTB's presentation. You may begin when you're ready.

MR. HUNTER: Okay. Thank you.

PRESENTATION

MR. HUNTER: If I can provide the Panel with a road map for this case in my presentation, here's where I'm going. I'll give you the background of this case, the facts that have been described, and then I will explain why the payments Appellant made on another's behalf fail

to qualify for a bad debt deduction. I'll explain why Appellant's cash transfers to the debtor failed to qualify for a bad debt deduction. And finally, I will explain why 2012 -- sorry -- 2013 -- 2012 is not the proper year to report a bad debt deduction and why this bad debt deduction was properly disallowed on the 2013 return.

And as we've heard, Appellant is the founder of the number one business management firm in this country, the Nigro Firm, which provides management services to high-net-worth individuals. During the time period at issue in this case, Appellant was a managing partner at the firm. Among the firm's clients were Ms. Barr and Mr. Thomas. The firm advised both Ms. Barr and Mr. Thomas to loan one Mr. Roberts, the debtor, $1 million each. They were told that they would receive an above market rate of return.

Ms. Barr made her loan in 2001. Mr. Thomas made his loan in 2002. However, Mr. Roberts, the debtor, failed to make any loan payments or interest payments on these loans. The Appellant stepped in and guaranteed the payment of Ms. Barr's loan in writing. He signed his guarantee personally, not in his capacity as partner of the Nigro Firm. That's at Exhibit D. Over time Appellant made payments totaling a net $600,000 on this guarantee. And by 2009, Mr. Thomas became concerned that he also had

not received loan repayments or interest payments on his loan.

Appellant has shown that he made a $700,000 payment directly from his bank account to Mr. Thomas along with other amounts recorded on his books, not the firm's books. And Mr. Thomas also acknowledged that Appellant made an investment on his behalf, Mr. Thomas, in the amount of $100,000. So in all, Appellant recorded almost $2 million of these payments that he made to Ms. Barr and Mr. Thomas on behalf of Mr. Roberts. He deducted this amount as a bad debt deduction on his 2012 income tax return, and he could not utilize this entire amount of these deductions on his 2012 return, and the majority was carried over to the 2013 return.

Appellant also deducted additional amounts that were for checks that he wrote directly to Mr. Roberts, the debtor, over the years. These checks had the word loan -- sorry -- the word "loan" written on the memo line and totaled $378,000. Appellant also reported this amount that he paid directly to Mr. Roberts as a bad debt. When Appellant's 2012 return came up for audit, the deductions were disallowed because Appellant provided no evidence for entering into the guarantee of Mr. Roberts' debt for profit or receiving reasonable compensation in return for entering into this guarantee of Mr. Roberts' debt to

Ms. Barr, and the other guarantee, which is not in writing for Mr. Thomas.

He had no legal obligation to provide this guarantee, and the regulations only can consider his payments to these lenders on Mr. Roberts' behalf as now a loan owed to him from Mr. Roberts only if certain conditions are met, and they're not met here. When Appellant's 2013 return came up for audit, these deductions were disallowed because Appellant failed to provide evidence supporting a bona fide debt for the cash outlays made from him to Mr. Roberts directly. There were promissory notes, but they were not interest payments made, no stated collateral, no collection efforts made, et cetera.

So as it comes to the guarantees, here the issue is whether Appellant is allowed a non-business bad debt deduction for his payment as a guarantor because there's no loan from him to Mr. Roberts in terms of these of guarantees. In the briefing, we listed the controlling non-exclusive factors considered by the Ninth Circuit Court of Appeals in determining whether parties intended to create a bona fide debt. And because we're speaking about a guarantee, when a taxpayer guarantees payments of the debts of another, payment on this obligation will give rise to a bad debt deduction only if the agreement was

entered into the course of taxpayer's trade or business or for profit.

Also there was an enforceable duty for the taxpayer as guarantor to make the payment, and the guarantee was entered into before the obligation became worthless. In other words, there was still a reasonable expectation of repayment by the original debtor, in this case Mr. Roberts, at the time the taxpayer entered into the guarantee. Appellant contends that he entered into the guarantees for profit as they would improve his business relationships with his clients through indirect consideration.

But the question is, where's his profit motive. If anything, he was attempting to make good on someone else's promise to repay, and the advice was provided to these clients by the firm. Mr. Roberts certainly did not provide Appellant with any consideration to enter into those guarantees. And also Ms. Barr and Mr. Thomas were clients of the firm. The firm could have backed up this bad investment advice.

Appellant in the Nigro Firm are separate taxpayers. The firm could have made things right for his clients. Or in the alternative, Appellant could have allowed Mr. Roberts to be accountable under the promissory note he signed with Ms. Barr and Mr. Thomas who would have

a legitimate bad deb deduction because they loaned money to someone and he did not repay. In terms of the loans made directly to Mr. Roberts by Appellant, he took the reporting position that these cash outlays were bona fide loans. And by 2012 and 2013, these loans were uncollectible.

A bona fide debt arise from a debt or credit relationship based on a valid and enforceable obligation to pay a fixed or determinable sum of money. And as stated in the briefing, these key factors, these non-exclusive factors under the Welch v. Commissioner, which would show that this is a valid and enforceable obligation are from missing here. Appellant produced copies of promissory notes signed by Mr. Roberts that obligated Mr. Roberts to repay him with a stated amount of interest.

Appellant also indicated here, and now in his testimony, that he has a longstanding history of dealing with Mr. Roberts. His promise was as good as gold to pay folks back who lent him money. Pre-1987 he was loaned $10 million and paid back every penny. And this subjective narrative happened long before the loans we are discussing in this case. And while looking at these non-exclusive factors in terms of whether a bona fide loan was established or not, we look at them from an objective

stand point, not from a subjective standpoint.

If you look at the history of the repayments in term of the line items that gave rise to the bad debt deduction in 2013 for the cash outlays that Mr. -- strike that -- that Appellant loaned to or gave to Mr. Roberts, they totaled $300,000 by 2004, yet, Appellant recorded receiving only one payment of $25,000. That's on a $300,000 outstanding obligation. And yet, Appellant still lent Mr. Roberts an additional $220,000 after that, receiving any repayment or interest payments subsequently.

There was no stated security or collateral provided for these loans. And Appellant keeps pointing to the ranch in Mandeville Canyon. I will get to our evidence that we provided that as early as 2009, this ranch -- this real estate asset was under water, and it was leveraged. For all these reasons, when viewed from an objective prospective, these checks that Appellant wrote to Mr. Roberts do not a qualify as a bona fide loan that give rise to a valid bad debt deduction.

Finally in terms of the tax year, we provided evidence that from an objective standpoint Mr. Roberts had no ability to repay his loans to Ms. Barr, Mr. Thomas, or Appellant as of 2010. Again, Mr. Roberts owned this real estate in Mandeville Canyon via his wholly-owned single member LLC, which failed to have met its financial

obligations to a venture capital firm, which foreclosed on the property.

We also submitted other evidence that over and above this Mandeville Canyon ranch, Mr. Roberts also had collection issues. We submitted a creditor's claim with a declaration of Dawn Ross who described how as early as 2003 she loaned the debtor $500,000, and she was forced to sue when he failed to repay the loan. She filed an action in the Los Angeles Superior Court. She had to enforce a settlement agreement. Sadly the debtor passed away, and she did not receive anything on this obligation. She had to open up an estate and file a creditor's claim. And it's my understanding she was not repaid.

Also we submitted a publicly filed document information that Mr. Roberts owed Respondent, the FTB, $2 million on sate tax liabilities going back as far as 1998 and 1999, which was filed in April of 2000 before any of these loans were made that we're discussing today.

And a quick comment in terms of Mr. Roberts filing a document disclosing cancellation of debt income. That really has no effect on this particular case. Mr. Roberts was insolvent. So he filed a document that acknowledged, "I have cancellation of debt income." But it did not offset any other income that he had. I could not find a tax return for the year this particular

document was filed. And while that may be an exhibit, I don't believe that turns this case.

Also, we submitted other documents in terms of filings at the courthouse. The debtor was sole shareholder of Kelsho Radio Group, Inc., which was an S corporation that owned 98 percent of Kelsho communications. Mr. Roberts the debtor himself as an individual held the remaining 2 percent. And that particular company was sued over nine times. I provided the docket of these collection cases out of the Los Angeles Superior Court. Mr. Roberts had judgments obtained against him by Palm Finance, the Jeffer, Mangels Firm, J-e-f-f-e-r, M-a-n-g-e-l-s Firm. RFF Family Partnership received an arbitration award. There were judgement debtor examines, et cetera.

These are documents filed at the courthouse. And when look at this from an objective standpoint, you -- strike that.

It is improper for a taxpayer to rely on a subjective history of monumental ups and downs when a third-party-neutral lender would not do the same in terms of making a bona fide debt to this particular debtor. Again, Appellant must show that the debt had value at the beginning of the year, the year the debt was reported, year 2012, and became wholly uncollectible by the end of

the year. The only movement here is Appellant's $700,000 that he made directly to Mr. Thomas in 2012 that has no bearing on Mr. Roberts ability to repay. There was no springing ability to repay in 2012.

Additionally, I believe this is an exhibit, in 2012 Appellant received an email from Mr. Roberts wherein Mr. Roberts indicated, "I'm working on a very few exciting projects."

And even Appellant discounted this by responding two minutes later in saying, "That doesn't help with the money you probably owe me."

So again, we submit that a neutral third-party lender would not loan this individual this amount of money when this individual has a demonstrated inability to repay especially, when this debtor already allegedly owes the lender several million dollars or even in the case here of $20,000 when Mr. Roberts' wholly-owned S corporation was forced into bankruptcy. They listed the Nigro Firm as a creditor for unpaid management fees.

Appellant indicated that he considered taking this bad debt deduction in 2010, but the only thing leading him not to take this bad debt deduction until 2012 were emails of conversations with Mr. Roberts. These are not reasonable collection efforts. A neutral third-party lender, a bank, would send a demand letter, would file a

complaint, would turn square corners to make things right and get their money back. So we submit that 2010 is the year of worthlessness when viewed -- when this situation -- when this record is viewed from an objective standpoint, which is what the law calls for.

Finally, I want to address something here which I think really needs to be discussed in order to clarify something. Appellant is an individual. This is his personal income tax return, and Ms. Barr, Mr. Thomas, even Mr. Roberts were client of the Nigro Firm. And when we're discussing a business risk for this financial advice, make these loans to Mr. Roberts and you will get an above market rate of return, whose risk are we discussing? Whose business risk? It is the firm.

So again, the firm could have made these right -- made this right or make payments on these outstanding obligations, written it off as a loss on the partnership return. If there's any affect of a loss that could be reported on Appellant's individual return, he would receive that via K-1. There are other ways this could have been done as opposing Counsel has presented other scenarios. However, we're discussing this case with this tax reporting position and what was done and how these line items do not qualify as a bad debt deduction.

So to ask the question what else could it have

been? I'm telling you what it's not. And again, the taxpayer when they reported bad debt deduction, they have to show and prove that they fall squarely within the perimeters of the deduction that the legislature has granted, and Appellant has not done so in this case.

Thank you.

JUDGE LONG: Thank you.

I'm going to turn to my panel members.

Judge Vassigh, do you have any questions for either party.

JUDGE VASSIGH: I do not. Thank you.

JUDGE LONG: Thank you.

And Judge Ridenour?

JUDGE RIDENOUR: I do. Thank you.

Mr. Segal, I have a question for you. For the record clarification, when you paid those debts THAT Mr. Roberts had to Ms. Barr and Mr. Thomas or Thompson -- I do apologize -- did you then create a loan document that Mr. Roberts signed that he was in debt to you for either or both?

MR. SEGAL: I truly don't recall. I can tell you he was fully aware, and he had fully acknowledged that he had owed me those monies in emails. But I don't recall whether we did provide a note or not.

There is one more important fact missing.

Mr. Thomas had lent money to Mr. Roberts seven or eight times prior to this and had been repaid in full with interest seven or eight times, which is a relevant fact to why he would lend somebody a million dollars.

JUDGE RIDENOUR: Oh, yeah. I'm not speaking about the loan between Thomas and Roberts. I'm more talking about when you covered the loan, if then you went to Mr. Roberts and said I'm covering this loan for you. Therefore, you have a loan to me, and here's the document creating that loan.

MR. SEGAL: I don't recall if that document exist, but the discussion clearly took place. And Mr. Roberts was fully aware that I had to repay those amounts.

JUDGE RIDENOUR: Okay. Thank you for the clarification. No more questions.

JUDGE LONG: Thank you.

Mr. Weintraub, you mentioned earlier that because 2012 is closed, whether that bad debt deduction is actually at issue.

I was wondering if Mr. Hunter could address that.

MR. HUNTER: Sure thing. This audit was conducted for both tax years 2012 and 2013, and it was taking a while and extension of the statute of limitations was signed, which was effective for tax year 2013. But

2012 was under review from the inception of the audit. And the bad debt deduction was determined to be unsupported and disallowed for tax year 2012. It was carried forward, the majority of it, and deducted giving rise to a tax effect in 2013. And that's why we're here today.

So Respondent does have the ability to adjust deductions when they were taken forward and applied to subsequent year. It's called an NPACA Notice of Proposed Amount -- no -- Noticed of Proposed Adjustment to carryover Amounts. So despite the tax year being closed, you're not getting the -- strike that.

The taxpayer is not receiving the benefit of the carryover until a subsequent year, which is the year at issue here. So the fact that the tax year was closed has no impact on the assessment that we're discussing here this morning.

JUDGE LONG: Thank you.

I'm going to quickly review my notes to make sure I have all my questions answered.

Mr. Weintraub, Mr. Hunter mentioned that in order to become worthless for a debt deducted in a particular year, the debt needs to have some value at the beginning of the year. If you could address that and whether the debts had, from Appellant's prospective, any value in the

beginning of 2012.

MR. WEINTRAUB: Yes. The corollary of that is that the debt had no value at the end of the year. So when Mr. Segal determined the end of 2012, the debt had no value. That means in his mind, based upon the history and course of conduct, up until then he believed that he would receive repayment. Whether it was 100 percent, 50 percent, he believed that Mr. Roberts was capable of paying a portion of the debt. And until it was clear that no portion could be paid, it was not properly deductible. So he believed that it had a value, that some value.

He would not have disposed of that receivable if someone said, "Mr. Segal I'll give you a dollar. You want to sell me your receivable for Mr. Roberts," he would not have. He believed he had a prospect of some payment at the beginning of the year. That's why the debt had value. If believed it had no value at the beginning of the year, he would have deducted it earlier. So he waited until he believed that there was no prospect and no -- and the value of the debt at that point had been reduced to zero.

JUDGE LONG: So I'm going to ask Mr. Segal. What led you to believe that the debt had value at the beginning of 2012?

MR. SEGAL: A 30-year history with this client where he went from inches of bankruptcy to worth of $100

million. There was no premise to believe he couldn't do it again. And he had ample opportunities in writing in these years between '10 and '12 to do it. And if history isn't a guide to this, then I don't know what it is. It's easy for the FTB to make an argument to fit their needs to their case, but that's not the reality.

Reality is what this client did for 30 years and multiple times in which he had zero to no net worth, and within periods of times after that he's worth hundreds of million dollars of dollars. There is no premise to believe that it couldn't happen again, and he was actively working on two or three real deals just like he had been before. There was no premise it couldn't happen again.

Not owning his home didn't affect his ability to do a transaction. And so I firmly believe that it could happen until he became so ill to the point where he couldn't do it. And that all occurred sometime in '12. And at that point it was pretty clear he's not going to make a transaction, and that's the point I took the deduction. I absolutely could have made the argument that the FTB is making, is that I could have took it in '10 because his house was gone, et cetera, which would have been only more beneficial to take it then.

It's earlier, and the benefits would have been earlier. But I didn't. And I didn't because it wasn't

nothing at that time. And the fact that he had foreclosures and he had liens and he -- he'd been there for 30 years. It wasn't anything different than he had before. And so I think that was -- I think that's the most important fact here. And, you know, it's easy. Hindsight is really strong, but living through it is very different.

And as I say, this client by far was the most resilient client in 44 years of business that I've seen. I can assure you that there were times that I thought there was no way nothing good was going to happen to this client, but every time that ended there he bounced back. And so there was no reason to believe he couldn't bounce back again. And that should be what the driving force is. Is it worth something or isn't it when you have a client that can go from zero to a hundred million. You have to be sure that can't happen anymore before you take a loss, and that's what we waited to do.

There was one other point that was relevant that I just wanted to make here as the taxpayer and Appellant here. Mr. Hunter stated that these loans that talked about, $10 million or more of repayment loans occurred in the first five, seven, eight years. That's actually, substantially incorrect. The loans occurred over a 20-plus year period of time in which people were repaid.

And it wasn't based on an event. It was based on cash flow that he had to repay them. And until that cash flow didn't exist, he was able to repay them.

And it's, you know -- look, I'm perfectly prepared. If you rule that I owe this money, I'll write a check. Not that I'm excited about it because I don't think I really did thinking wrong. And helping a client isn't exactly doing something wrong. It's what we're engaged to do. The other thing that's farly [sic] misstated by Mr. Hunter is when partners represent clients, they may end up with the risk of the results of that representation.

I've been the managing partner of this firm for 42 years. And partners multiple times have self-funded errors that they made with their clients that resulted a need to pay something. It could have been a tax liability. Unlikely. It could have been an investment that they went into that didn't work, and the clients were repaid. Those partners paid it directly multiple times. To argue that the business had to pay it in order to make it business related is ridiculous.

If I left the firm the next day and went across the street, I'd be in the same business with the same clients. So paying a debt for that client is absolutely normal and common. And I don't know where Mr. Hunter

would know that it isn't. I can assure you in my firms it's happened a dozen times in 42 years. Nobody is happy about it, but they do the right thing. They made the mistake. They step up and make the mistake and they make those transactions. And that's what I did here to protect this business and all my other partners and employees, and it's the right thing to do.

JUDGE LONG: Thank you.

I'm going to turn to Judge Ridenour for additional questions.

JUDGE RIDENOUR: Yes, I have a couple of more questions for you, Mr. Segal. Can you clarify for the record when exactly Mr. Roberts became ill?

MR. SEGAL: I believe he became ill in the beginning -- the middle of 2011, and I'm defining he became when they began to run some tests on him. They didn't have any answers until at least March of 2012 where they began to say you know what, all these avenues went down are wrong. It appears you have stomach cancer, and we need to verify that. That led to some other kinds of cancer, and it was a fight he wasn't going to win. And that's when I knew it in 2012.

JUDGE RIDENOUR: Thank you. Also I was wondering, so you said there was ample opportunity for him to be able to repay you that was in writing, if I

understand what you just said.

MR. SEGAL: Well, one of the emails was read in which he said I'm working on multiple things at the time, and that was a '12 email. You ask -- I mean, I'm trying to give you a feel for this client. It's not like no other client. And so he literally could make a deal in a six-month time period that generates a hundred million dollars because of who he is and the people he worked with. So we got something in early in '12 that said the door is not closed. Don't give you up. It could happen. But as he got sicker and sicker, it was clearly evident. And even if he believed he could do it, it wasn't going to happen. And by the end of '12 he was pretty sick.

JUDGE RIDENOUR: So in the email, which we have, he doesn't really give specifics as to what he's working on and his projected income for these. So did you just rely on his generalization?

MR. SEGAL: 30 years of performance is what I relied on.

JUDGE RIDENOUR: Okay. And then follow-up question, did you make any efforts? Like, did you say I need this payment or I need a payment by X date? It's been two years or it's been one year. I understand he was a client, so I understand that there was this history. But he also went without repaying all this time.

MR. SEGAL: There are multiple emails asking him how are you going to repay? When will you be able to repay? You know, keep in mind Mr. Hunter believes this is some kind of federal banking transaction. This private lending. It doesn't fit under anything he quoted. Because a bank requires collateral doesn't mean a private lender requires collateral. And so look, it's very easy to drive facts to tell your story. It's very different to live the story. Okay.

And the fact of the matter is when you've repaid $12 million, $10 million of loans with interest over a 20-plus year period of time, even clients who lent, right, they didn't even chase notes. They call got him because he wouldn't take the money in without them in these cases. But they didn't ask for notes. It was a good arrangement for him and a good arrangement for them until it wasn't. And in the end, there was really only a few people holding a bag. Two of them were clients, one was myself, and one was my partner.

And as I said to you before, my partner was audited and with no change. So, again, I work in this business. I file 7,000 tax returns every year for clients. If they owe the money, they should pay the money. And I'm telling you as you sit there, if you decide it's my fault, I was wrong in what I did, I'll

write the check.

But I will tell you I do this all the time for a living. I lent these people money. I covered his debt 'cause I had no choice. And the fact that you want to argue -- that FTB wants to argue your business should have did it, that's a ridiculous position. If I leave, my clients go with me. They aren't owned by the business in any way shape or form nor are any of my partner's clients. And that's why you often --

JUDGE RIDENOUR: Mr. Segal, I'm going to --

MR. SEGAL: Go ahead.

JUDGE RIDENOUR: You've more than answered any question.

MR. SEGAL: Okay.

JUDGE RIDENOUR. Thank you very much. And I would like to say however the Panel decides, it's not so much you did something wrong. It's just that we have to look at the record and to make sure that the statutory requirements are met. So I just wanted to say that as well.

MR. SEGAL: The only question I'll leave on the table, the FTB has yet to answer on a hundred requests, what is it if it isn't a loan. It seems to me that's a fair question to get an answer for. Yet, they've never answered that question in six years of this process.

JUDGE RIDENOUR: Thank you. I'm done with my questions.

JUDGE LONG: I have I think one last question. So Appellants have stated that the repayment to Mr. Thomas could also alternatively be considered a loan by Mr. Segal. What is FTB's position on that instead of a guarantee?

MR. HUNTER: Well, we disagree with that contention. I believe the question was asked, did you have him sign a promissory note for $700,000 in the year 2012, and the answer is no. And when you look at the factors as discussed by the Welch case by the Ninth Circuit, was there an ability to repay $700,000 -- strike that.

Did Mr. Roberts have the ability to repay Appellant $700,000 in tax year 2012 when Appellant made that cash transfer, wrote that cashier's check to Mr. Thomas? So no. I mean, that's -- when someone is here presenting before you and said alternatively it could happen X, that is the not the reporting position. And it's Respondent's position that it still did not support a bad debt deduction on Appellant's personal income tax return for the year.

Thank you.

JUDGE LONG: Thank you. All right.

Mr. Weintraub, you have five minutes if you want to address any additional issues or for a rebuttal. You can take this time now.

MR. WEINTRAUB: Okay. Thank you.

CLOSING STATEMENT

MR. WEINTRAUB: Just a few highlight points. What we're talking about here is an economic loss suffered by a taxpayer of monies that were paid out and not repaid. And if they're treated as loans, the law provides a deduction for a bad debt. And we've heard this morning that the FTB doesn't have a different characterization. I think the statement was, "I know what it's not," which was to say the FTB's contention that it's not a loan. But there is no other characterization.

Whether there was documentation, security, interest, his course of conduct is what controls the characterization. It could have been oral. It could have simply been a check with a notation. It's the understanding and the agreement of the parties that characterizes the transaction, to not held slavishly to formalities of third-party lenders and documentation.

If the money transferred looked like a loan and was treated like a loan, it is a loan, even without a promissory note. There was no reason for Mr. Segal to

advance funds on behalf Mr. Roberts. It wasn't a gift. He didn't acquire anything. The understanding of the parties was Mr. Segal is making an additional advance for the benefit of Mr. Roberts. They had a long history. They were close. They trusted one another.

The formalities wouldn't have changed it. It wouldn't have suddenly imbued that with reality as a loan when the course of conduct provides that and the case law supports that. And the fact that there isn't anything else it could be, has to mean that it's a loan. So we have a loss suffered on funds provided as loans. There's nothing else it could be, and we're dealing with the year in which this loss which should be treated.

I also wanted to clarify this point about the cancellation of debt. I think it requires some explanation. Cancellation of debt, when a taxpayer is relieved of the obligation to repay is treated ordinarily as income. The federal purpose is Section 10 -- Section 61 that provides cancellation of debt. It's an economic increment to net worth. But if an individual is insolvent at the time of cancellation or in bankruptcy, under Section 108, the law provides you don't have to report that as income. You can exclude because it would be silly and counter productive to tax somebody when they have no net worth.

So in the case of Mr. Roberts, yes, he had cancellation of debt income, but it wasn't taxable income. It was excludable under Section 108. But the price that you pay for the benefit of excluding cancellation of debt income is to give back any of the tax benefits you've been holding onto. So if you had a net operating loss carry forward, if you had a capital loss carry forward, if you own depreciable real property, you have to make an adjustment. You have to give that back. And that's what was reported in 2000 -- on Mr. Roberts' 2012 return.

He didn't report income because he qualified for the exclusion under Section 108. But to the extent he had any tax attributes, he had to give those up dollar for dollar. For every dollar of income that was excluded, he had a reduced tax attribute. So he had a net operating loss. It was gone. If he had a capital loss carryover, it was gone. If he had depreciable real property, he would had to have reduce the tax basis of the property.

So the parties reported it that way. That was further evidence of the parties, Mr. Roberts and Mr. Segal agreeing as to what the relationship was. There's a long history of loans, and this was a cancellation of a loan. A cancellation of debt with or without a promissory note. It doesn't make it more or less a loan when the parties' conduct establishes that it's a loan.

And finally as to the 2012 year, what's anomalous is that if Mr. Segal had capital gains in 2012 and used the losses that he reported against those capital gains, reduced the income, he would have received the benefit of those losses. The FTB had the opportunity to audit and disallow the bad debt deduction claimed in 2012 and did not do so. The fact that he carried it over to 2013 should not deprive him of a loss that was not challenged, whether you want to take the position that they didn't challenge the characterization as a bad debt.

They didn't challenge the characterization as a bona fide loan. They didn't challenge the characterization that 2012 was the proper year. They didn't do it. They had the -- that's what statutes of limitations are for so you're not endlessly exposed to audits for things that are in the past. So this was claimed in 2012. The FTB had the opportunity. They were looking at it. Maybe they made a mistake. Maybe it was an oversight. But it didn't, and they should not be able to come into 2013 and say well, wait a minute. That loss in a closed year, we don't think that was a bona fide debt. And even if it was, we don't think that was the right year. You should have claimed it earlier. Well, you should have disallowed it earlier.

It's the same argument. The statute is closed.

Just like Mr. Segal can't go back to 2010 and claim the deduction because it's closed. FTB shouldn't be able to go back to 2012 and now say well, we don't like the treatment. We don't think it's a bona fide debt. We don't think 2012 is the right year. The opportunity was there, but it's closed.

So for all of these reasons, we do think that Mr. Segal did it properly. He waited until it was absolutely clear that his loans -- and again, they were loans. They were nothing else -- could not be collected, and then he deducted them. I don't know what else he's supposed to do. I don't know what else the taxpayer is supposed to do. Could he have been more rigorous in the documentation of the loan? Sure. But it wouldn't have changed anything. And after all the years and all the loans and all the repayments, he didn't need that documentation to establish that the relationship of the funds transferred by him to Mr. Roberts were loans.

And that's all -- that's all that we have here are loans that were made. They were not repaid. There was a loss. Nobody is disputing that there was a loss. Nobody is disputing the amounts. What we're sitting here arguing is was it a bona fide debt? We say it was. Was 2012 the proper? We think conservatively that was the proper year, and that's what was deducted.

Thank you.

JUDGE LONG: Thank you.

I'm going to turn to my Panel members one last time to see if they have any additional questions.

Judge Vassigh?

JUDGE VASSIGH: I do not have any questions. Thank you.

JUDGE LONG: And Judge Ridenour?

JUDGE RIDENOUR: No further questions. Thank you.

JUDGE LONG: All right. That will conclude the hearing for this hearing. I will be deciding this case based on the briefings and the arguments presented, Appellant's testimony, and the admitted evidence. And we will have the written opinion out no later than 100 days from today.

Thank you again for your participation today. The case is now submitted, and the record is closed.

The Office of Tax Appeals will now be in recess until 1:00 p.m. Thank you.

(Proceedings adjourned at 11:00 p.m.)

HEARING REPORTER'S CERTIFICATE

I, Ernalyn 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 25th day of September, 2023.

_____
ERNALYN M. ALONZO
HEARING REPORTER