

BEFORE THE OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

IN THE MATTER OF THE APPEAL OF,)
)
J. ERSKINE and H. ERSKINE,) OTA NO. 220911516
)
 APPELLANT.)
)
)

TRANSCRIPT OF ELECTRONIC PROCEEDINGS

State of California

Friday, September 22, 2023

Reported by:
ERNALYN M. ALONZO
HEARING REPORTER

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Transcript of Electronic Proceedings,
taken in the State of California, commencing
at 1:04 p.m. and concluding at 1:29 p.m. on
Friday, September 22, 2023, reported by
Ernalyn M. Alonzo, Hearing Reporter, in and
for the State of California.

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APPEARANCES:

Panel Lead: ALJ NATASHA RALSTON

Panel Members: ALJ ANDREA LONG
ALJ ANDREW KWEE

For the Appellant: J. ERSKINE

For the Respondent: STATE OF CALIFORNIA
FRANCHISE TAX BOARD
BLAKE CUNNINGHAM
CHRISTOPHER TUTTLE

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I N D E X

E X H I B I T S

(Appellant's Exhibit 1 was received at page 7.)

(Department's Exhibits A-G were received at page 7.)

P R E S E N T A T I O N

P A G E

By Mr. Erskine	9
By Mr. Cunningham	15

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P A G E

By Mr. Erskine	19
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California; Friday, September 22, 2023

1:04 p.m.

JUDGE RALSTON: And we are opening the record in for the hearing Appeal of Erskine, Office of Tax Appeals Case No. 22091156. Today's date is September 22nd, 2023, and the time is approximately 1:04 p.m.

My name is Natasha Ralston, and I'm the lead Administrative Law Judge who will be conducting the hearing for this case. We also have Judge Long and Judge Kwee on this Panel. You'll notice that the composition of this Panel has changed since the prehearing conference on August 30th, 2023. Judge Kwee has been added to the Panel, and I have been moved to the lead ALJ.

Does either party have an objection to these panel changes?

Mr. Cunningham?

MR. CUNNINGHAM: No.

JUDGE RALSTON: No objection.

And Mr. Erskine, no objections?

MR. ERSKINE: Yes. No objection.

JUDGE RALSTON: Thank you. Thank you very much.

As you are aware, this hearing is being live streamed to the public and is being recorded. The transcript and the video are part of the public record and

1 will be posted on the Office of Tax Appeals website.

2 Also present is our stenographer, Ms. Alonzo, who
3 is reporting this hearing verbatim. To ensure that we
4 have an accurate record, we ask that everyone speaks one
5 at a time and does not speak over each other, and also
6 speak clearly and loudly. When needed, Ms. Alonzo will
7 stop the hearing process and ask for clarification. And
8 after the hearing, Ms. Alonzo will produce the official
9 hearing transcript, which will be verifiable on our Office
10 of Tax Appeals website.

11 As you're aware, the Office of Tax Appeals or OTA
12 is an independent government agency and is not a Tax
13 Court.

14 So a few matters to discuss before we get into
15 the hearing. The prehearing conference in this matter was
16 held, I believe, in August 30th. And at that point,
17 Appellant Mr. Erskine submitted one exhibit that was
18 54 pages and is labeled Exhibit 1. At the time, FTB did
19 not object to Appellant's exhibit.

20 Is that still correct, Mr. Cunningham?

21 MR. CUNNINGHAM: Correct. No objection.

22 JUDGE RALSTON: Thank you.

23 So Appellant's Exhibit 1 is admitted without
24 objection.

25 ///

1 (Appellant's Exhibit 1 was received in
2 evidence by the Administrative Law Judge.)

3 JUDGE RALSTON: So FTB had submitted Exhibits A
4 through F, and Appellant did not have any objections at
5 that time. Respondent FTB subsequently entered Exhibit G,
6 which is part of the Exhibit E to Appellant's
7 S corporation return.

8 Mr. Erskine, did you receive that Exhibit G that
9 FTB submitted? It was around September 6th they submitted
10 it.

11 MR. ERSKINE: I've received quite a bit. I mean,
12 what is it?

13 JUDGE RALSTON: It looks like it was Exhibit E
14 from the S corporation return.

15 MR. ERSKINE: Okay. I think that's -- yeah, I
16 do.

17 JUDGE RALSTON: Okay. Did you have any
18 objections to any of FTB's exhibits?

19 MR. ERSKINE: I do not.

20 JUDGE RALSTON: Okay. Thank you.

21 So FTB's Exhibits A through G are admitted
22 without objection.

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

25 JUDGE RALSTON: Looks like Respondent doesn't

1 intend to call any witnesses, but Appellant is intending
2 to testify under oath or affirmation.

3 Respondent does not object to that; is that
4 correct?

5 MR. ERSKINE: Correct.

6 JUDGE RALSTON: Mr. Cunningham?

7 MR. CUNNINGHAM: No objection.

8 JUDGE RALSTON: Thank you.

9 Mr. Erskine, before you go into your testimony, I
10 will have you sworn in. And after that, FTB or the Panel
11 may have some questions for you. So I will let you know
12 when that will be. It will be in a few minutes.

13 Mr. Erskine will have 10 minutes to present the
14 case and testimony. Respondent will also have
15 approximately 10 minutes to present their case. And then
16 Mr. Erskine will have 5 minutes for a rebuttal or closing
17 statement.

18 Does anyone have any questions?

19 Looks like no one is indicating that they have a
20 question, so we're going to move on to the opening
21 presentations.

22 Mr. Erskine, can you raise your right hand so I
23 can swear you in.

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J. ERSKINE,

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

JUDGE RALSTON: Okay. Thank you. You have about 10 minutes for your presentation. So please begin when you're ready.

PRESENTATION

MR. ERSKINE: Yeah. I'll make it pretty simple from my side.

The entity, the income that come to me personally, first of all, so that there's clarity, is a variety of investment vehicles that there's large fluctuations of cash flow and income. And year to year it's very -- it's very -- it's not a consistent business. You know, it's a -- it's one of the larger business that behind it is lending business and, you know, for -- it's mortgage related. So, you know, the -- you can have years that are very good, and you can have years like now that are extremely bad.

My team that works with me and organizes tax and income, you know, made -- including, I think, participated in or, you know, whatever that means from the previous

1 year's tax returns, you know, had that any sort of overage
2 go into the following year. You know, we know
3 miss historically, unless we know there's a big difference
4 in year after year, we follow the estimated payment
5 schedule that, from my understanding, is, you know,
6 something like 90 or something percent of the previous
7 year's tax liability or something that we follow and, you
8 know, we made our quarterly payments.

9 And the reason that we challenge this is that,
10 you know, we really had no way of knowing the fluctuation
11 of income because the vast majority of the income that was
12 earned and reported and coming through a K-1, that
13 business is not an active business. It's just an
14 investor. So we didn't receive -- because of Covid we
15 didn't receive K-1s on that entity and didn't really even
16 know the income from that entity until well into 2021.
17 You know, there's a variety of K-1s, which I'm sure the
18 tax return reflect.

19 And I am by no means a CPA, so I'm not going to
20 pretend to know every detail that's on there. But, you
21 know, they were coming in, and the largest amount of the
22 income was coming in. It was received on September 15th,
23 2021. So, you know, literally just -- they're very, very
24 late into the year.

25 One other point with that is, you know, although

1 it may seem like to some as an immaterial amount or as an
2 immaterial amount relative to the income, you know, what's
3 also important to understand is that we're -- these
4 entities are partnerships. So this is not income that's
5 coming to me in the form of true income. What actually is
6 received in the form of distributions is oftentimes just
7 enough to cover the actual income.

8 So the income coming through is just related to
9 my -- to these entities. Partnership interests in these
10 entities, and it's the pass-through income that's
11 associated with it. And then depending on the cash flow
12 of these businesses, you know, the distributions are
13 nowhere near, not even close to the level of income that's
14 showing there. And in some cases, it's not even enough to
15 cover the tax liability because the businesses are growing
16 businesses.

17 So I just wanted to point that out, although I
18 wouldn't think that would weigh on the decision of the
19 judges on the Panel that sometimes when maybe somebody
20 sees large amounts of income that it come across that
21 there's, you know, an equally amount of cash that's
22 sitting in the account to pay that. And that's just not
23 true. We do distributions very differently in those
24 businesses and oftentimes, the distributions are barely
25 there to cover the tax liability, which is why we've

1 challenged this because we feel that they're not
2 businesses that we have that the entity knows what the
3 income is going to be.

4 It's very difficult to estimate. And when the
5 K-1s come in, we feel like we made, you know, payments as
6 quick as we possibly could once the accountants put
7 together the K-1s from the multitude of entities. I think
8 that we, you know, historically had made our estimated
9 payments. And then the following year, you know, we way
10 overpay because of making the estimated payments. It's
11 just clockwork.

12 So I don't have really a lot more to talk about
13 because the point that I have challenged this on is just
14 that I wouldn't have known the income. This is not an
15 active business. These are passive businesses. There's a
16 bunch of K-1s that come in and get compiled to figure it
17 out. And we were making estimated payments based on the
18 previous year's income. And Covid created an absolute
19 anomaly for several of the businesses because it created,
20 you know, the busiest year and the highest income year
21 that business has ever seen. But, again, didn't come
22 with -- unfortunately, it doesn't come with the
23 distributions to cover, you know -- that all that income
24 isn't being distributed out.

25 So my -- my case is just purely based on it. I

1 made my estimated payments based on previous year. This
2 is not a -- this is a business that is getting K-1s that's
3 flowing into my personal income, but it's coming through,
4 basically, trusts that get distributed. So if you look,
5 there's a layered -- there's a bunch of entities. It goes
6 into an entity and that money gets distributed out through
7 trusts that I pick up the income from. And it's a lot of
8 K-1s, and it gets compiled. I made the estimated
9 payments. The K-1s came very late in the year, and I made
10 the payments within a very short period of time.

11 So I felt the penalties that I paid for that --
12 because we had an inability to estimate the income --
13 couldn't do it any differently today if I tried. You
14 know, we're punitive to the point that I felt it was worth
15 the time to go through this process and challenge it.

16 So that's -- that's all I have to say.

17 JUDGE RALSTON: Okay. Thank you, Mr. Erskine.

18 FTB, did you have any questions for the
19 Appellant?

20 MR. CUNNINGHAM: This is Blake Cunningham
21 speaking. I have no questions.

22 JUDGE RALSTON: Thank you. I'm going to check
23 with my Panel.

24 Judge Long, did you have any questions for
25 Mr. Erskine.

1 JUDGE LONG: This is Judge Long. I have no
2 questions at this time.

3 JUDGE RALSTON: Thank you. And Judge Kwee, did
4 you have any questions at this time for Mr. Erskine?

5 JUDGE KWEЕ: Hi. This is Judge Kwee. I did have
6 one question. I'm wondering if you received any income
7 estimates earlier in the year before the schedule K-1 was
8 finalized?

9 MR. ERSKINE: No. We received -- because of the
10 way -- we oftentimes quite honestly like, you know, for an
11 example, this year we just got our K-1s for one of the
12 main businesses. We just figured out the income six days
13 ago for 2022. We don't receive any estimates because it
14 fluctuates significantly. And the auditors -- because
15 it's part of a multitude of different businesses, that the
16 auditors decide -- because oftentimes there's
17 consolidation going on, that it greatly fluctuates things.
18 And at the end of the year, there's evaluations given to
19 the assets on the balance sheets on loans being held, and
20 that oftentimes gets changed by the auditors and the third
21 parties by the time it's done.

22 So we get -- we receive no estimates throughout
23 the year. In fact, we oftentimes get the -- our first
24 estimate we try to get -- we sometimes receive in March or
25 April of the following year, but we truly don't know our

1 actual income until the K-1 comes out. And this year, a
2 good example being, it was seven days ago for last year.

3 JUDGE KWEE: Okay. Thank you. I don't have any
4 further questions.

5 I'll turn it back to you Judge Ralston.

6 JUDGE RALSTON: Okay. Thank you, Judge Kwee.

7 And thank you, Mr. Erskine.

8 FTB, you have about 10 minutes. Please begin
9 when you're ready.

10

11 PRESENTATION

12 MR. CUNNINGHAM: Good afternoon.

13 My name is Blake Cunningham, and I am here with
14 Topher Tuttle, and together we represent Respondent
15 Franchise Tax Board.

16 So the issues before us today are whether
17 Appellant has met their burden of proof to establish
18 reasonable cause to abate the late payment penalty, and
19 whether Appellants have established a legal basis to abate
20 the estimated tax penalty.

21 For taxable year 2020, Appellant filed their
22 return timely on extension, October 15th, 2021. On the
23 return, Appellants reported tax due that they didn't pay
24 on time. The remaining tax balance was paid with their
25 return. Since Respondent did not receive full payment by

1 the due date of the return, May 17th, 2021, Respondent
2 imposed a late payment penalty. In addition, since
3 Appellant did not make sufficient estimated tax payments,
4 they were assessed an estimated tax penalty. They were
5 also assessed applicable interest.

6 So first regarding the late payment penalty,
7 since Appellants' unpaid tax was five months late,
8 pursuant to Revenue & Taxation Code Section 19132,
9 Respondent imposed a \$5,008 late payment penalty. The law
10 presumes the late payment penalty was imposed correctly.
11 So to overcome this presumption, Appellants must establish
12 their failure to timely pay was due to reasonable cause
13 and not willful neglect that occurred, despite ordinary
14 business care and prudence.

15 The amount of the penalty is not in dispute.
16 However, Appellants assert that the late-payment penalty
17 should be abated because for reasonable cause, because the
18 payments were reasonable based on revenue from previous
19 years. In addition, Appellants argue that they did not
20 know the business income until they received the K-1s in
21 September of 2021. It should be noted that Appellants'
22 primary source of income is from the K-1 issued to
23 Appellants reporting nonpassive income of approximately
24 \$4.3 million from at Teton Global Investments, LLC, in
25 which Appellant is president and 50 percent shareholder.

1 Appellant has been signed the return. Thus,
2 since Appellants were actively involved in the business,
3 an ordinary, intelligent, and prudent business-person
4 exercising ordinary care in the same situation would have
5 reasonably known how much income would be allocated to
6 them. In addition, even if Appellant was unsure of the
7 income amount, Appellants have not met their burden
8 because they have provided no evidence to establish what
9 efforts they took to ascertain the income amount in order
10 to be eligible to pay by the due date of the original
11 return, which would be January 1st through May 17th date.
12 For these reasons, the late payment penalty should be
13 sustained.

14 Next, regarding the estimated tax penalty
15 pursuant to California Revenue & Taxation Code
16 Section 19136, a taxpayer is required to make payments of
17 the estimated amount of their tax when they receive income
18 not subject to sufficient withholding. The failure to
19 timely pay estimated tax will subject the taxpayer to an
20 estimated tax penalty. In this case, Respondent imposed a
21 \$3,434 estimated tax penalty because Appellants did not
22 pay enough estimated tax for the 2020 taxable year.

23 Appellants do not contest the imposition or
24 computation of the estimated tax penalty but assert
25 reasonable cause for the same reasons as discussed in the

1 late payment penalty. However, the imposition of the
2 estimated tax penalty is mandatory. Unlike the late
3 payment penalty, it cannot be abated upon showing of
4 reasonable cause or lack of willful neglect. In certain
5 situations, the estimated tax penalty may be abated if by
6 reason of casualty, disaster, or other unusual
7 circumstances. The imposition of the penalty would be
8 against equity in good conscience.

9 However, this exception for unusual circumstances
10 is considerably narrower than reasonable cause.
11 Appellants have not provided evidence demonstrating that
12 this limited exception applies to their situation as they
13 have made the same reasonable cause argument as discussed
14 under the late payment penalty. Accordingly, Appellants
15 have not established the legal bases to abate the
16 estimated tax penalty.

17 In conclusion, Appellants have not established
18 reasonable cause to abate the late payment penalty and
19 have not established a legal basis to abate the estimated
20 tax penalty. Based on these reasons, Respondent ask that
21 its actions denying Appellants' refund claim be sustained.

22 Thank you, and I'll be happy to answer any
23 questions.

24 JUDGE RALSTON: Okay. Thank you, Mr. Cunningham.

25 Judge Long, did you have any questions for

1 Respondent?

2 JUDGE LONG: This is Judge Long. I do not have
3 any questions. Thank you.

4 JUDGE RALSTON: Thank you.

5 Judge Kwee, did you have any questions for
6 Respondent?

7 JUDGE KWEE: Hi. This is Judge Kwee. I do not
8 have any questions. Thanks.

9 JUDGE RALSTON: Okay. Thank you.

10 Mr. Erskine, you have five minutes for a
11 rebuttal.

12

13 CLOSING STATEMENT

14 MR. ERSKINE: A couple of things to just point
15 out from the -- from the feedback here. The Teton Global
16 Investments, where the income comes in is also a
17 partnership, and that's not an entity that operates. The
18 two owners of Teton Global Investments are actually not
19 me. It's my -- it's a trust that -- and again, I'm not a
20 CPA expert in this. You know, attorneys and CPAs have the
21 structure in place. I receive the income because I'm the
22 one that receives the income distributed through the
23 trust.

24 Teton Global Investments is actually owned 50
25 percent by my trust and 50 percent by my brother's trust,

1 and that entity is an entity that operates. It has no
2 employees. It has a management contract to manage the
3 investments, and all of the income that comes into Teton
4 is coming in the form of K-1s from other entities. And so
5 we don't have the means even if -- number one, we're not
6 owners of that, our trust are. And number two, that
7 entity does not do business, and it doesn't have a means
8 of being able to estimate income because that entity is
9 just receiving K-1s from investment income from entities
10 that it owns interest in, and that's where it receives it.

11 So far as just because we're -- we're stated to
12 be 50 percent owner, yes, I receive 50 percent of the
13 income, but my trust is actually the owner of it and I'm
14 just a decision -- I'm a trustee for the trust. I'm a
15 trustee for my brother's trust, and he's a trustee for my
16 trust. But the income comes down through because of how
17 the trust is set up. I just want to make it clear that
18 entity is not an operating entity, and that entity
19 wouldn't have any knowledge of income -- unless to
20 Judge Kwee's point -- the entities gave estimated payments
21 throughout the year. Of which I can say on the record,
22 none of the K-1s that come into Teton Global Investments,
23 I can -- I don't think I've ever seen an estimated payment
24 before, what I mentioned earlier, which was after the tax
25 year of an estimation of income that comes from any of the

1 because that Teton owns an interest in. So I just want to
2 clarify that point.

3 And then the second point on the disaster. You
4 know, I think that Covid was pretty rampant, right. Like
5 everything was impacted by Covid that year. I mean
6 absolutely everything. Nothing was normal. Our business
7 income wasn't normal. The way our taxes were done weren't
8 normal. In jurisdictions where I lived, taxes were
9 extended to be filed by December instead of October. I
10 mean, nothing was normal that year. The CPAs were not
11 able to get through the work on time on reduced workloads.

12 So I would state on the second point that
13 although, you know, the main point being that I had no way
14 of knowing the income or else we would have paid it. Our
15 history is that we pay, and that's supported by which --
16 you know, there's probably no evidence of it here, but in
17 2021 we made a gross overpayment of probably a
18 million-plus dollars because we were following that same
19 philosophy. I would say that the point being on the other
20 one is that there was a disaster that year and nothing was
21 normal. Getting anything out of companies and CPAs and
22 anything just didn't happened.

23 So that's my only comments. Thank you for your
24 time.

25 JUDGE RALSTON: Thank you.

1 I'm going to check with my Panel again to see if
2 there's any questions.

3 Judge Long, did you have any questions for either
4 party?

5 JUDGE LONG: This is Judge Long. I do not have
6 any questions. Thank you for your time.

7 JUDGE RALSTON: Thank you.

8 And Judge Kwee, did you have any questions for
9 either party?

10 JUDGE KWEE: Hi. This is Judge Kwee. I'm ready
11 to conclude. I don't have any further questions. Thank
12 you.

13 JUDGE RALSTON: Okay. Thank you everyone.

14 Today's hearing in the Appeal of Erskine is now
15 adjourned, and the record is closed.

16 So the Judges will meet and decide your case
17 later on, and we will send you a written opinion of our
18 decision within 100 days.

19 Thank you everyone for attending.

20 I just want to double check. I think that's it
21 as far as hearings go for today. So we will go ahead and
22 conclude. Thank you everyone.

23 (Proceedings adjourned at 1:29 p.m.)
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HEARING REPORTER'S CERTIFICATE

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

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

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

I have hereunto subscribed my name this 24th day
of October, 2023.

ERNALYN M. ALONZO
HEARING REPORTER