

**OFFICE OF TAX APPEALS**  
**STATE OF CALIFORNIA**

In the Matter of the Appeals of: ) OTA Case Nos. 21067893, 21118984,  
T. ABRAMSON, ) & 21119139  
A. ABRAMSON, )  
D. TEIGER, AND )  
S. WEINTRAUB-TEIGER )

**OPINION ON PETITION FOR REHEARING**

Representing the Parties:

For Appellants: Kreig D. Mitchell, Attorney

For Respondent: Nathan H. Hall, Attorney Supervisor  
Jason Riley, Attorney

V. LONG, Administrative Law Judge: On December 14, 2023, the Office of Tax Appeals (OTA) issued an Opinion sustaining the actions of respondent Franchise Tax Board (FTB) denying T. Abramson, A. Abramson, D. Teiger, and S. Weintraub-Teiger’s (appellants’) claims for refund for tax years 2013 through 2017.

In the Opinion, OTA held that the architectural firm of Abramson Teiger Architects, LLP (ATA) was not entitled to research and development (R&D) tax credits that it claimed for tax years 2013 through 2017. Appellants timely filed a petition for rehearing (petition) under Revenue and Taxation Code (R&TC) section 19334. Upon consideration of appellants’ petition, OTA concludes that appellants have not established a basis for rehearing.

A rehearing will be granted where one of the following grounds for rehearing exists and materially affects the substantial rights of the party seeking a rehearing: (1) an irregularity in the appeal proceedings which occurred prior to issuance of the Opinion and prevented fair consideration of the appeal; (2) an accident or surprise, occurring during the appeal proceedings and prior to the issuance of the Opinion, which ordinary caution could not have prevented; (3) newly discovered evidence, material to the appeal, which the party could not have reasonably discovered and provided prior to issuance of the Opinion; (4) insufficient evidence to justify the

Opinion; (5) the Opinion is contrary to law; or (6) an error in law in the OTA appeals hearing or proceeding. (Cal. Code Regs., tit. 18, § 30604(a)(1)-(6); *Appeal of Do*, 2018-OTA-002P.)

In their petition, appellants request a rehearing on the basis that there was insufficient evidence to justify the Opinion, and the Opinion was contrary to law.

### Insufficient Evidence

To find that there is insufficient evidence to justify the Opinion, OTA must find that, after weighing the evidence in the record, including reasonable inferences based on that evidence, OTA clearly should have reached a different opinion. (Code Civ. Proc., § 657;<sup>1</sup> *Appeals of Swat-Fame Inc., et al.*, 2020-OTA-045P.) OTA considers the evidence in the light most favorable to the prevailing party (here, FTB). (*Appeal of Shanahan*, 2024-OTA-040P.)

Appellants contend that there is insufficient evidence to justify the Opinion because: the Opinion erred in attributing an assertion to appellants that they did not make; the Opinion made incorrect assumptions of fact not in evidence; appellants satisfied the “substantially all” rule and the recordkeeping requirement; the Opinion erred in concluding that the timekeeping records do not allow OTA to apply the shrinking-back rule; and the Opinion erred by not addressing the burden-shifting to FTB given that appellants provided credible evidence.

### Contrary to Law

The contrary to law standard of review involves reviewing the Opinion for consistency with the law. (Cal. Code Regs., tit. 18, § 30604(b).) The question of whether the Opinion is contrary to law requires a finding that the Opinion is “unsupported by any substantial evidence;” that is, the record would justify a directed verdict against the prevailing party. (*Appeal of Martinez Steel Corporation*, 2020-OTA-074P.) This requires a review of the Opinion in a manner most favorable to the prevailing party and indulging “in all legitimate and reasonable inferences” to uphold the Opinion. (*Ibid.*; see also *Appeals of Swat-Fame Inc. et al., supra.*) The question does not involve examining the quality or nature of the reasoning behind OTA’s Opinion, but whether the Opinion can or cannot be valid according to the law. (*Appeal of*

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<sup>1</sup> As provided in *Appeal of Wilson Development, Inc.* (94-SBE-007) 1994 WL 580654, it is appropriate for OTA to look to Code of Civil Procedure section 657 and applicable caselaw as relevant guidance in determining whether a ground has been met to grant a new hearing.

*Martinez Steel Corp., supra.*) OTA considers the evidence in the light most favorable to the prevailing party (here, petitioners). (*Appeal of Shanahan, supra.*)

Appellants contend that the Opinion is contrary to law because: the Opinion erred in finding that appellants had the burden of proof on new issues raised by FTB on appeal; the Opinion made incorrect assumptions of fact not in evidence; and appellants satisfied the “substantially all” rule and the recordkeeping requirement.

#### Eligibility for the Research and Development Tax Credit

As stated in the Opinion, to be eligible for an R&D tax credit under Internal Revenue Code (IRC) section 41(a)(1), as modified by R&TC section 23609, appellants must prove that ATA performed qualified research, or paid someone else to perform qualified research, during the years at issue.<sup>2</sup> Qualified research is research that satisfies four tests:<sup>3</sup>

1. Section 174 Test: expenditures connected with the research must be eligible for treatment as expenses under IRC section 174 (IRC, § 41(d)(1)(A));
2. Technological in Nature Test: research must be undertaken for the purpose of discovering technological information (IRC, § 41(d)(1)(B)(i));
3. Business Component Test: the taxpayer must intend that the information to be discovered be useful in the development of a new or improved business component (e.g., a product, technique, formula, or invention) of the taxpayer (IRC, § 41(d)(1)(B)(ii)); and
4. Process of Experimentation Test: substantially all of the research activities must constitute elements of a process of experimentation for a purpose relating to a new or improved function, performance, reliability, or quality (IRC, § 41(d)(1)(C), 41(d)(3)).

The above tests are applied separately to each business component. (IRC, § 41(d)(2)(A).) A “business component” is defined as “any product, process, computer software, technique, formula, or invention” which is to be “held for sale, lease, or license” or “used by the taxpayer in a trade or business of the taxpayer.” (IRC, § 41(d)(2)(B).) If a business component as a whole fails the qualified research tests, a court may apply the “shrinking-back rule,” which allows the

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<sup>2</sup> Appellants do not claim to have paid any third parties to perform qualified research.

<sup>3</sup> For purposes of the California research credit, “qualified research” only includes research conducted in California. (R&TC, § 23609(c)(2)(A).)

court to apply the qualified research tests to a subset of the business component if doing so will allow the subset to satisfy those tests. (Treas. Reg. § 1.41-4(b)(2).)

1. Burden of Proof on New Issues

Appellants contend that the Opinion is contrary to law because it erred in determining that FTB had not presented a new matter. However, the Opinion's determination was supported by relevant case law and applicable evidence, including the Audit Issue Presentation Sheet (AIPS) issued by FTB. Specifically, the Opinion analyzed relevant case law in determining that whether a new assertion constitutes a new matter turns on whether the new assertion "merely clarifies or develops the original determination without being inconsistent or increasing the amount of the deficiency." (*Achiro v. Commissioner* (1981) 77 T.C. 881, 890.) The Opinion evaluated the AIPS and determined that issues raised in FTB's opening brief require the same presentation of evidence as FTB requested of appellants at audit. Accordingly, the determination is not contrary to law because it is not "unsupported by any substantial evidence." (*Sanchez-Corea v. Bank of America* (1985) 38 Cal.3d 892, 907 (*Sanchez-Corea*).)

In addition, the Opinion did not sustain FTB denying appellants' claim for refund based on the purported new assertions. Rather, the Opinion held that appellants failed to establish that ATA engaged in research activities of which "substantially all" constituted a process of experimentation and that appellants did not provide sufficient evidence/records to allow OTA to apply the shrink-back rule. Thus, even if appellants were correct that FTB's funded research and copyright arguments were considered new matters of which FTB had the burden of proof, it would have no impact on the outcome of the appeal.

2. Assertions Attributed to Appellants

Appellants contend that there is insufficient evidence to justify the Opinion because it erred in attributing an assertion to appellants that appellants did not make. Specifically, the Opinion states "[a]ppellants asserted during the hearing that all of the claimed work hours are qualified hours because the employees were working on qualifying projects." Appellants contend that they did not make this assertion, but instead asserted that a subset of the hours and activities for qualified projects was used to compute the research tax credits. Appellants further detail that non-qualified time was removed from qualified projects using "detailed contemporaneous timesheet records."

The Process of Experimentation Test requires that “substantially all” of a taxpayer’s research activities constitute elements of a process of experimentation for a purpose relating to a new or improved function, performance, reliability, or quality. (IRC, § 41(d)(1)(C), 41(d)(3).) This test is applied separately to each business component. (IRC, § 41(d)(2)(A).)

In appellants’ petition, they state “[b]ecause [a]pellants did not claim the credit for any research activities that did not constitute [Process of Experimentation] research activities, appellants’ percentage of [Process of Experimentation] research activities to total research activities is, therefore, 100% far exceeding the substantially all requirement.” Accordingly, it appears that appellants contend that, because they only included qualified hours in their claim, that all of their claimed hours are qualified hours. Appellants made this same argument on appeal, and was considered in the Opinion in conjunction with the evidence provided by appellants to substantiate their research activities, namely, the testimony of Mr. Abramson and the timesheet records. The Opinion evaluated this evidence and appropriately determined that appellants had not provided sufficient evidence to show that the claimed qualified hours were spent on qualifying projects constituting qualified research activities involving a process of experimentation, let alone meeting the “substantially all” test. An examination of the evidence in the record, including reasonable inferences based on that evidence, does not show that OTA clearly should have reached a different opinion. (Code Civ. Proc., § 657; *Appeals of Swat-Fame Inc., et al., supra.*)

### 3. Assumptions of Fact Not in Evidence

Appellants contend that the Opinion is contrary to law and that there is insufficient evidence to justify the Opinion because the Opinion made incorrect assumptions of fact not in evidence. Appellants take issue with a statement made in the Opinion when discussing whether substantially all of ATA’s research activities constituted a process of experimentation. The Opinion states that the hourly detail information provided by appellants was vague; “[f]or example, the employees could be working on elements of design that do not contain uncertainties, such as landscaping, roofing materials to use, etc.” Appellants take issue with this statement because they contend that it is contradicted by evidence including witness statements, photographs, renderings, other “project documents,” and timesheet records.

However, the statement appellants refer to is not included in the Opinion’s factual findings; rather, it is in the discussion to illustrate the vagueness of appellants’ timekeeping

records and failure to meet their burden of demonstrating entitlement to the R&D tax credit. The Opinion evaluated the evidence, particularly Mr. Abramson’s testimony and the timesheet records, and determined that the evidence was too vague (i.e., the timesheet entries included descriptions of work such as “design meeting” and “go through keynotes for plans”) to substantiate that ATA engaged in research activities, “substantially all” of which constituted a process of experimentation. An examination of the evidence in the record, including reasonable inferences based on that evidence, does not show that OTA clearly should have reached a different opinion. (Code Civ. Proc., § 657; *Appeals of Swat-Fame Inc., et al., supra.*) Further, the determination is not contrary to law because it is not “unsupported by any substantial evidence.” (*Sanchez-Corea, supra.*)

4. “Substantially All” Rule and Recordkeeping Requirement

Appellants contend that the Opinion is contrary to law and that there is insufficient evidence to justify the Opinion because appellants satisfied the “substantially all” test and the recordkeeping requirement. Appellants contend that their timesheet records and witness testimony are sufficient to substantiate the claimed work hours for research tax credit purposes. Appellants assert that the Opinion’s reliance on *Little Sandy Coal Company, Inc. v. Commissioner* (7th Cir. 2023) 62 F.4th 287 is misplaced because, unlike the taxpayer in that case, appellants have timesheet records. Appellants further contend that testimony alone is sufficient to establish claimed work hours, citing *Amazon.com & Subsidiaries v. Commissioner* (2017) 148 T.C. 108, *U.S. v. McFerrin* (5th Cir. 2009) 570 F.3d 672, and *Suder v. Commissioner* T.C. Memo 2014-201.

In determining whether relief should be granted, the relevant question is not over the legal quality or nature of the reasoning behind an opinion, but whether the opinion can or cannot be valid according to the law. (*Appeal of Swat-Fame, Inc., et al., supra.*)

The Opinion discussed the sufficiency of appellants’ timesheets and testimony to evaluate whether appellants had demonstrated that ATA engaged in research activities, “substantially all” of which constituted a process of experimentation. In evaluating appellants’ timesheets, the Opinion stated “[...] the descriptions of work performed are vague, (e.g., ‘team meeting to review drawings and discuss week’s schedule,’ ‘design meeting,’ ‘go through keynotes for plans,’ etc.).” Thus, the issue was whether appellants had shown that ATA engaged in research activities that constituted a process of experimentation. Since the Opinion

determined this initial step of demonstrating qualified research activities had not been met, the Opinion did not further analyze whether appellants had demonstrated the amount of qualified wage expenses (i.e., the amount of time employees spent on such qualified research activities).

To the extent that appellants assert that testimony alone is sufficient to establish ATA's qualified research activities, OTA has held that even in the case of credible testimony, such as Mr. Abramson's, "[The testimony] either alone or together with the other evidence, did not provide sufficient detail to satisfy the [...] qualified research tests." (*Appeal of First Solar, Inc.* 2023-OTA-532P.<sup>4</sup>) Here, the Opinion considered Mr. Abramson's testimony and concluded that it was insufficient to establish that ATA's engaged in research activities, "substantially all" of which constituted a process of experimentation. While the authorities cited by appellants suggest that testimony alone *may*, in certain instances, be found sufficient to establish claimed work hours for research credits, OTA is not required to accept such testimony where, as here, OTA finds the testimony lacking in sufficient detail to satisfy that "substantially all" of the claimed research activities constituted a process of experimentation.

#### 5. Shrinking-Back Rule

Appellants contend that there is insufficient evidence to justify the Opinion because the Opinion erred in determining that the record did not allow OTA to apply the shrinking-back rule. Appellants contend OTA could have applied the shrinking-back rule using the hours per phase set out in the AIPS or by comparing data provided in appellants' exhibits.

The Opinion analyzed the evidence provided and stated that it was unable to apply the shrinking-back rule because of "appellants' strategy in recordkeeping by project and phase, [lacked] detail of time spent on specific activities [...]." In their petition, appellants fail to identify any subparts to which the shrinking-back rule could be applied to for application of the "substantially all" test. For the same reasons as discussed above, evidence can be used to estimate qualifying wages only after a taxpayer has established that it engaged in qualified research activities. Appellants failed to identify and substantiate the precise activities which constituted a process of experimentation and, therefore, qualified research activities. As a result, OTA cannot reasonably estimate the qualified wages associated with those activities. After

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<sup>4</sup> See Treas. Reg. § 1.41-4(d), stating that "[a] taxpayer claiming a credit under [IRC] section 41 must retain records in sufficiently usable form and detail to substantiate that the expenditures claimed are eligible for the credit."

weighing the evidence in the record, appellants have not shown that OTA clearly should have reached a different opinion.

6. Burden-Shifting

Appellants contend that there is insufficient evidence to justify the Opinion because the Opinion did not address the burden shifting to FTB based on appellants' presentation of evidence. As stated in the Opinion, tax credits are a matter of legislative grace, and taxpayers bear the burden of proving they are entitled to the claimed tax credits. (*Appeal of Swat-Fame, Inc, et al.*, 2020-OTA-046P.) Statutes granting tax credits are to be construed strictly against the taxpayer with any doubts resolved in FTB's favor. (*Ibid.*) The taxpayer has the burden of showing that the requirements for the research credit are satisfied. (*Ibid.*) OTA's regulations provide that the burden of proof requires proof by a preponderance of the evidence. (Cal. Code Regs., tit. 18, § 30219(b).)

The Opinion did not address burden-shifting from appellants to FTB because appellants have the burden of proving entitlement to the deduction, and the Opinion determined that appellants had failed to meet their burden of proof. The Opinion found appellants' evidence insufficient to establish their entitlement to the claimed research credits.<sup>5</sup> Accordingly, the burden was not shifted to FTB in the appeal.

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<sup>5</sup> Appellants contend that they "presented credible evidence in this case as to the qualification of research activities and expenses," so the burden should shift to FTB based on IRC section 7491 ["if...a taxpayer introduces credible evidence...the Secretary shall have the burden of proof"].) However, California does not conform to IRC section 7491.



Accordingly, OTA finds that appellants have not satisfied the requirements for granting a rehearing and, as such, their petition is denied.

Signed by:  
*Veronica I. Long*  
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Veronica I. Long  
Administrative Law Judge

We concur:

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*Sheriene Anne Ridenour*  
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Sheriene Anne Ridenour  
Administrative Law Judge

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Administrative Law Judge

Date Issued: 10/9/2024