BEFORE THE OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

IN THE MATTER OF THE APPEAL OF,)
)
G. HYATT,) OTA NO. 22039964
)
APPELLANT.)
)
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TRANSCRIPT OF PROCEEDINGS

Sacramento, California

Tuesday, April 21, 2026

Reported by:
ERNALYN M. ALONZO
HEARING REPORTER

BEFORE THE OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

IN THE MATTER OF THE APPEAL OF, G. HYATT, APPELLANT.	OTA NO. 22039964

Transcript of Proceedings, taken at 400 R Street, Sacramento, California, 95811, commencing at 1:05 p.m. and concluding at 2:10 p.m. on Tuesday, April 21, 2026, reported by Ernalyn M. Alonzo, Hearing Reporter, in and for the State of California.

APPEARANCES:

Panel Lead:	ALJ HUY "MIKE" LE
Panel Members:	ALJ JOSH ALDRICH ALJ CHERYL L. AKIN
For the Appellant:	MATHEW CARLSON
For the Respondent:	STATE OF CALIFORNIA FRANCHISE TAX BOARD NOEL GARCIA-ROSENBLUM BRAD COUTINHO

I N D E X

E X H I B I T S

(Appellant's Exhibits 1-10 were received into evidence at page 6.)

(Department's Exhibits A-K were received into evidence at page 6.)

OPENING STATEMENT

CLOSING STATEMENT

Sacramento, California; Tuesday, April 21, 2026

1:05 p.m.

JUDGE LE: We are opening the record in the Appeal of G. Hyatt. This matter is being held before the Office of Tax Appeals. The OTA Case Number is 22039964. Today's date is April 21st, 2026, and the time is 1:05 p.m. This hearing is being held in person in Sacramento, California.

Today's hearing is being heard by a panel of three Administrative Law Judges. My name is Mike Le, and I will be the lead judge. Judge Cheryl Akin and Judge Joshua Aldrich are the other members of this tax appeals panel. All three judges will meet after the hearing and produce a written opinion as equal participants. Although the lead judge will conduct the hearing, any judge on this panel may ask questions or otherwise participate to ensure we have all the information needed to decide this appeal.

Now, for the parties introductions, for the record, will the parties please state their names and who they represent, starting with Respondent.

MR. GARCIA-ROSENBLUM: Noel Garcia-Rosenblum, representing Respondent Franchise Tax Board.

MR. COUTINHO: Good afternoon. Brad Coutinho, also representing Respondent Franchise Tax Board.

JUDGE LE: Thank you.

And turning to Appellant.

MR. CARLSON: Matthew Carlson on behalf of Appellant Gilbert Hyatt.

JUDGE LE: Thank you. Thank you both.

Let's move on to my Minutes and Orders. As discussed with the parties at a prehearing conference on March 16, 2026, and notated in my Minutes and Orders, the issue in this appeal is whether OTA has jurisdiction to review the post-amnesty penalty imposed under R&TC section 19777.5. During the presentation, the parties may provide a brief statement outlining how they think the issue should be phrased in this appeal. Appellant's Exhibits 1 through 10 were entered into the records in my Minutes and Orders.

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

JUDGE LE: Respondent's Exhibits A through K were also entered into the record in my Minutes and Orders.

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

JUDGE LE: No witnesses will be testifying at this hearing. Both parties submitted a list of names and cases to the stenographer, so thank you both.

And let's see. After the prehearing conference, Appellant submitted a motion to compel. As to the supervisory approval aspect of the post-amnesty penalty, Respondent replied, and Respondent stated that "Written supervisory approval of the post-amnesty penalty imposed on Appellant was not and cannot be obtained." So, I believe that resolves the parties' dispute as to that matter.

Let me first turn to Respondent.

Any questions or comments before we begin with Appellant's presentation?

MR. GARCIA-ROSENBLUM: No questions. Thank you.

JUDGE LE: And turning to Appellant.

Any questions or comments before you begin with your presentation?

MR. CARLSON: No questions, Your Honor. Thank you.

JUDGE LE: Okay. And with that, the time is 1:07 p.m. You have up to 25 minutes. Please begin.

MR. CARLSON: Thank you, Your Honor.

PRESENTATION

MR. CARLSON: Respondent Franchise Tax Board has recently admitted that it did not get written supervisory approval for the post-amnesty penalty in this case.

Section 19187(b) requires all penalties to be approved in writing by a supervisor, unless the penalties meet narrow exceptions that do not apply in this case. Because Respondent did not get written supervisory approval, the post-amnesty penalty is invalid.

OTA has jurisdiction to hear this case because its timely appeal from a timely refund claim. OTA has the authority to enforce the written supervisory approval for requirement because it is a statutory element of the post-amnesty penalty. Respondent should have accountability for failure to follow the mandatory supervisory approval requirement, and OTA should hold that the post-amnesty penalty --

JUDGE LE: I'm sorry. Can you move the microphone a little bit closer to you.

MR. CARLSON: Oh, I'm sorry. You can't hear.

JUDGE LE: Thank you.

MR. CARLSON: Okay. So, first, OTA should follow the federal precedent in this case. So, supervisory approval is a statutory element of the penalty claim, and OTA can enforce it in the same way that the federal courts have been enforcing this element for years at the federal level. So first, California law has long held that federal decisions interpreting substantially identical federal statues are unusually strong persuasive precedent on the construction of California provisions; and that's People versus Hagen.

The same rule applies for federal regulations. So, federal regulations also apply in interpreting California statutes where the federal and state statutes are substantially identical, and that's the Rihn versus Franchise Tax Board case. In both, the federal case law and the federal regulations are relevant in this case for a few reasons. First, the federal case law makes clear that the supervisory approval elements, it's an element of the penalty; and that comes from that Chai opinion.

Federal case law also holds that the written supervisory approval and retirement can be enforced in cases even where the penalty cannot otherwise be challenged on the merits. And also in cases where the taxpayer is not allowed to raise the usual defenses to a penalty. That comes from the ATL and Sons case and also, the Patel cases. And finally, both federal case law and federal regulations provide that a penalty is only accepted from the written supervisory approval requirements if the penalty is proposed in a notice generated by a by computer without human involvement. This is an extremely narrow exception that does not apply in this case, and this comes from the Walquist versus Commissioner case in final Regulation under 6751(b).

And so, 6751(b) of the Internal Revenue Code and then 19187(b) of the Revenue & Taxation Code are substantially --

JUDGE ALDRICH: Mr. Carlson?

MR. CARLSON: Yes.

JUDGE ALDRICH: Sorry to interrupt, but could you slow it down a bit for --

MR. CARLSON: Oh, am I going fast?

JUDGE ALDRICH: -- the Hearing Reporter?

MR. CARLSON: Sure. Yeah. Of course. Of course.

So -- so, these supervisions are substantially identical, the federal and state supervisory approval provisions. If you take a look at Exhibit A to Appellant's reply brief, there's a chart or a table. You can see the language side by side. It's nearly verbatim. This is because the state supervisory approval requirement was modeled after the federal provision. So, 19187(b) was part of Senate Bill 94, which provided specified conformity to the Federal Restructuring and Reform Act of 1998, which enacted 6751(b). So, OTA should follow the federal courts here in enforcing the written supervisory approval requirement because federal courts have spent a lot of time analyzing the penalty approval language over the last 10 years.

So, in general, in both the deficiency cases and post-assessment proceedings, like, collection due process cases, the -- the Tax Court has consistently enforced this requirement. And so -- and the Tax Court invalidates the penalty if it hasn't been followed. So, the Tax Court initially grappled with the issue of whether 6751(b) could be enforced at all in prepayment deficiency proceedings. But ultimately, in the Chai case, the Second Circuit found that the written supervisory approval requirement is an element of the penalty claim as long as the electronic means exception does not apply.

And so, a quote from that opinion it said, "The Second Circuit held the written approval requirement of 6751(b)(1) is appropriately viewed as an eliminate of a penalty claim and therefore, part of the IRS's prima facie penalty case," end quote.

And so, the current state of the federal law is that if the penalty was not approved in writing, that's the end of the inquiry. The penalty is invalid because this is a threshold element. And so, the Tax Court does not address any other elements in the penalty like, negligence or substantial understatement or fraud. The Tax Court doesn't get into any defenses to the penalty, like computational defenses or reasonable cause or good faith. The court simply invalidates the penalty once that threshold element is not satisfied.

So, OTA should construe 19187(b) the same way that the federal courts have construed 6751(b). Written supervisory approval is a statutory element of the penalty claim in this case, and the penalty cannot be sustained without it. The cases cited by Respondent in its briefs regarding the post-amnesty penalty just simply don't deal with this issue. You know, one thing to note is that the supervisory approval requirement, it's an element of the penalty. It's not -- it's not a normal defense. And so, this isn't like reasonable cause or a good faith. The case is cited in Respondent's briefs. They say this over and over again that OTA does not have jurisdiction to determine that there is a reasonable cause or a good faith exception to the post-amnesty penalty.

Other common defenses that aren't available, include substantial authority, reliance on tax advice, inadequately disclosed tax positions. So, none of these defenses appear in the post-amnesty penalty provisions anywhere. However, even without these defenses, the supervisory approval requirement is very different. It's the threshold elements of the penalty claim against the taxpayer. And this is from the Chai case and other federal cases. And because the supervisory approval requirement is -- it's a statutory element of the penalty, the Tax Court has the authority to enforce it, even where the taxpayer is specifically precluded by statute from disputing that penalty or from raising defenses to it.

And so, we have a couple of examples that are relevant at the federal level. We've got 6330(c)(2)(B). That's in the collection due process context. It says that a taxpayer cannot challenge an underlying liability if the Tax Court already had a prior opportunity to dispute the penalty or the liability, and it precludes the taxpayer from running -- raising any other defenses to it. So, the taxpayer is not able to raise reasonable cause or good faith if the taxpayer already had a prior opportunity to dispute the penalty. And -- and yet, the Tax Court has still found that if the IRS has not obtained written supervisory approval for a penalty, the penalty is invalid.

So, this is very similar to the restrictions that we have in this case. So, there's a restriction to penalty defenses for the post-amnesty penalty, and -- and it's a very comparable provision at the federal level. And so -- so the CDP, the collection due process context, we have a situation where the Tax Court has successfully harmonized competing provisions in the Internal Revenue Code, and has given effect to both provisions. So the Tax Court easily could have side-stepped this issue and said the taxpayer can't dispute this penalty because the taxpayer had a prior opportunity under section 6330(c)(2)(B), but the court still found a way to read both statutes together, and to read -- and to give effect to both provisions, even though there was some tension between the two statutes.

Another example from the -- from the federal case law is the Patel case. So, Patel involved economic substance penalties. And for these penalties, Congress has specifically eliminated reasonable cause and good faith defenses to that penalty. And yet, the Tax Court still found the IRS failed to comply with 6751(b), and this is for penalties that don't have the normal defenses available. And it makes sense because the written supervisory approval requirement is an element of the penalty claim. And the Patel case illustrates that supervisory approval is a distinct issue from penalty defenses. It goes to the threshold validity of the penalty. It's an element of the penalty.

And so, these cases show that, you know, the OTA can easily find a way to harmonize these competing provisions and give effect to both, even though the provisions have some tension.

Pardon me for a moment.

So, in summary, on -- on the federal precedent issue, OTA should follow federal precedent here in enforcing the written supervisory approval requirement in this case because 6751(b) and 19187(b) are substantially identical. And federal case law and -- and regulations are unusually strong persuasive authority in this context. OTA should follow the federal cases and regulations by giving effects to 19187(b) as an element of the post-amnesty penalty, and finding that the penalty is invalid in this case. So that's -- that's the federal -- federal precedent.

I want to parse the language of section 19777.5(e) a little bit more closely and talk about a case that -- that gets into that kind of language. So, Respondent cites several OTA opinions stating that the general rule -- the general rule that a refund may only be allowed on the grounds that the post-amnesty penalty was not properly computed. And there are also no exceptions for reasonable cause or good faith, and this is from the Kiss opinion; and other opinions say the same thing. But none of these cases that -- none of the cases cited by Respondent address the supervisory approval issue in that context.

And so again, 19187(b) is very different than standard penalty defenses because it is elements of the penalty claim rather than a defense, like reasonable cause or a good faith. And so useful case that does parse the same kind of penalty defense limitation language is in Kimberly Clark. So, Kimberly Clark discusses OTA's authority to consider penalty defenses in the large corporate underpayment penalty context. So, the LCUP penalty has the same defense limitation language. It says, "A refund may only be allowed on the grounds that the amount of the penalty was not properly computed by the Franchise Tax Board," and that comes from section 19138 subdivision (e); and this -- I call it defense limitation language.

This -- this language from the LCUP penalty provisions is almost identical to the post-amnesty penalty language, which is contained in 1977.5(e). It's -- the language is nearly verbatim. And so even though the LCUP penalty has this, you know, language limiting defenses, the LCUP penalty also has several statutory exceptions. So section 19138 provides no penalty shall be imposed on any understatement to the extent the understatement is attributable to a change in law, or the imposition of an alternative apportionment, or allocation method by the FTB, a change in the federal accounting method, or reasonable reliance on written advice of the Franchise Tax Board.

And so, these are all statutory components of the

LCUP penalty. There's specific codified exceptions. So, even though reasonable cause and good faith are not codified exceptions to the penalty, there are -- there are penalty defenses available. And these statutory exceptions all use the same prohibitive language. They all say no penalty shall be imposed. And that's the same language that appears in 19187(b) under the supervisory approval requirement. And so, for the LCUP penalty, it says no penalty shall be imposed if any of the exceptions apply." Just like section 19187(b) says no penalty shall be imposed if the written supervisory approval is not obtained.

And so, the use of the prohibitive language reiterates why the tax court has held that the supervisory approval requirement is a threshold element for penalties. And if the element is not satisfied, the remedy is that the penalty must be invalidated because it specifically says no penalty shall be imposed. And so going back to Kimberly Clark, the OTA in that opinion restates the general rule that the LCUP penalty can only be challenged on computational grounds, and that there is so reasonable cause exception.

And so shouldn't that be end of the inquiry, if the LCUP penalty can only be challenged on computational grounds? It seems like that should be the end of the opinion and yet, the OTA does not stop there. The OTA goes on to discuss and make specific findings about the statutory exceptions to that penalty. So, OTA ended up holding that none of the four statutory exceptions were applicable, but this holding wasn't just a passing reference to the exceptions in the opinion. OTA pointed out on three separate occasions that none of these four exceptions apply.

And so why would OTA bother to consider these statutory exceptions if 19138(e) limits OTA's authority or jurisdiction for the LCUP penalty to computational issues only? And so a reasonable reading of that case and of this language is that while subdivision (e) may limit OTA's ability to consider penalty defenses, like reasonable cause and good faith, OTA still must consider other statutory elements or components or exceptions to the penalty. So, in OTA, Kimberly Clark had to consider and determine whether the statutory exceptions to the LCUP penalty applied, even though the defenses to that penalty are specifically restricted. So, Kimberly Clark illustrates that OTA does not have to read 1977.5(e) to erase other statutory components of the penalty.

OTA gave effect to both provisions in Kimberly Clark by finding that subdivision (e) did not allow OTA to create a reasonable cause exception, but is also held and made findings that these other statutory exceptions were not applicable. And so that analysis makes sense because otherwise, this defense limitation language that we have in the post-amnesty provision, it would eat up these statutory exceptions and render them meaningless.

So, in Appellant's case, the supervisory approval requirement, it's a statutory element of the post-amnesty element; and that comes from Chai. And that's just like the exceptions to the LCUP penalty in Kimberly Clark where they were statutory components of the LCUP penalty. One thing to note about Kimberly Clark is that the taxpayer's argument was that the FTB didn't include certain information about the penalty or provide an explanation of the penalty in a notice, but that's -- that's a different issue. It doesn't -- it -- there's no case law holding that a failure to include information in a notice create results in elements for the penalty. Whereas, in -- in the case of written supervisory approval, there's significant authority holding that the failure to obtain approval results in the invalidation of the penalty.

The case is cited by Respondent in the amnesty penalty context repeatedly state the proposition that there's no reasonable cause; there's no good faith exceptions. And that makes sense, but even if reasonable cause and good faith can't be read into the code section as defenses, other statutory elements or components of the penalty still have to be considered; and this is consistent with federal law.

So, the Tax Court treats supervisory approval as statutory threshold element of penalties even where the merits of the penalty are not at issue, and even where reasonable cause or good-faith defenses are not available to the taxpayer. And so the take away on this point is that Kimberly Clark illustrates that even where there's language limiting refund defenses, OTA can still consider other statutory components to the penalty, including exceptions or statutory elements of the penalty, even if the OTA does not have authority or jurisdiction to apply a reasonable cause or good faith defense.

So, in -- I want to talk about the Burlington case and some other principals related to the Burlington case. So, OTA should harmonize these statutes, rather than erasing 19187(b). OTA does not have to apply 1977.5(e) in a way that would render the written supervisory approval requirement meaningless. So, the supervisory approval requirement, it's an element of the penalty, and so OTA should maintain its integrity in this case. Taxpayers faces with this penalty don't have the -- they don't have the ability to challenge the penalty until after it's already been imposed and paid in full.

Deficiency proceedings are not applicable to this penalty.

And so, if the FTB does not get supervisory approval of the penalty, the taxpayer would be left without a mechanism to dispute a statutory element of the penalty. And this would be contrary to the Kimberly Clark case that specifically considered other statutory elements of -- of the penalty. These sections can and should operate together without displacing one another, and they should be harmonized just as the Tax Court has harmonized potentially conflicting federal provisions.

And so, this is where the Burlington case is helpful to consider. Burlington tells us that OTA as an agency has the authority to refuse to enforce a statute in a way that would be inconsistent with another statute. Burlington also says that if statutes are so inconsistent that OTA cannot enforce both, OTA could decide which to enforce. And this goes to OTA jurisdiction. OTA does have jurisdiction or authority to consider how to enforce statutes that are potentially inconsistent. So, if necessary, OTA could decide not to enforce subdivision (e) to the extent it purports to erase supervisory approval requirement.

And so this is supported in Burlington and also, Attorney General Opinion 23-701, which said OTA has authority to find a tax regulation that would conflict with the statute and decline to apply that regulation. And that Attorney General Opinion cites Burlington as authority for that proposition.

This -- this isn't necessary in this case because the statutes can easily be harmonized. We've seen the Tax Court do it at the federal level with similar competing provisions, and OTA can do the same thing here. Supervisory approval is a statutory element of the penalty claim. So, OTA can determine whether it has been satisfied, the same way that OTA considered whether the statutory exceptions to the LCUP penalty applied in Kimberly Clark. Burlington also says there is a strong presumption against repeal by application. It only -- it only occurs where two statutes are so inconsistent that there's no possibility of concurrent operation, or the latter statute gives undebatable evidences of an intent to supersede the earlier statute. Burlington also states courts are bound to maintain the integrity of both statutes if they may stand together.

Same rule applies at the federal level. So, the Williams versus Commissioner case states that it is the duty of courts to give effect to both statutes. And in that case, Williams was construing section 6751(b). The post -- post-amnesty penalty and the supervisory approval statutes can both stand together. The federal cases show that similar provisions can easily be harmonized and can work together and courts can give effect to both. Subdivision (e) should not be read to -- to imply a repeal of section 19187(b) because there is a strong presumption against appeal by implication. And so there is no undebatable evidence of an intent to supersede section 19187(b).

And so, under Burlington, OTA can find a way to maintain the integrity of both statutes in this case. They're not too inconsistent to work together. And so, the takeaway is that OTA should hold subdivision (e) limits OTA's authority or jurisdiction to consider usual penalty defenses like reasonable cause or good faith, but that supervisory approval remains a threshold element for the valid imposition of any penalty. And so, this is a reasonable reading that allows both statutes to operate concurrently, which is the stated goal in Burlington. And so, Appellant is not asking OTA to ignore or invalidate subdivision (e). OTA can construe it so it does not erase section 19187(b), and that is permissible under Burlington.

I want to move on to the question of whether one 19187(b) applies to the post-amnesty penalty. In general, a written supervisory approval is a procedural requirement for all penalties, unless accepted -- the post-amnesty penalty is not specifically accepted. It does not fall under the narrative definition of a penalty automatically calculated by electronic means. Section 19187(b)(1) says no penalty under this part shall be imposed unless the initial determination is personally approved in writing by the immediate supervisor of the individual making that determination.

And so, the post -- the post-amnesty penalty, it's a penalty under the same part as 19187 -- 19187(b). Both are contained in part 10.2. The specific exceptions listed in 19187(b)(2) are specific, and the post-amnesty penalty is not concluded on that list as an exception. And the penalty does not fall under the narrow exception for penalties automatically calculated through electronic means. This is a narrow section that -- sorry. It's a narrow exception that only applies to automated penalty notices generated entirely by computers. And we know this because it comes from the federal definition.

In this case, we know that FTB employees and not computers manually generated -- generated the relevant penalty notices, both before and after the penalty was imposed. And going through the notices on Exhibit C through G in Appellant's reply, Respondent did not allege that any of these were generated by a computer with the exception of Exhibit G, which was allegedly system generated. But that penalty was issued well after the penalty had already been imposed. So, it's not relevant. Through informal discovery, Respondent didn't identify which employee prepared any of the notices.

So, we can't tell who the employees were or who their supervisor might have been, but we don't need to determine who actually approved the -- or who should have approved the penalty because Respondent has conceded that the penalty was never approved in writing. So regardless, under the federal definition, the post-amnesty penalty is not calculated by electronically -- sorry -- calculated automatically by electronic means because humans generated the notices proposing the penalties, not computers. In its briefs, Respondent contends that the penalties are mathematical in nature and therefore, should be considered accepted from -- from the written supervisory approval requirement.

But all penalties are mathematical in nature. Computers are used to calculate every penalty. Nobody at the FTB is calculating them with a pencil, so mathematical in nature. It's just not -- it's not the test. The test is whether the penalty is automatically calculated through electronic means, and that only applies to fully automated penalty notices. Respondent also contends the post-amnesty penalty is mandatory. There's no discretion to impose the penalty, but that's not the test either.

So -- so, all penalties are definitely mandatory because they all say shall be imposed. None of them say may be imposed at the FTB's discretion, but that does not mean -- go ahead.

JUDGE LE: We are now over the 25-minute mark. Please try to wrap up your presentation, Mr. Carlson.

MR. CARLSON: Sure. Sure. Sure.

JUDGE LE: Thank you.

MR. CARLSON: And so being mandatory is not the test. And so -- but the penalty isn't mandatory really anyway. Section 19735 says FTB may issue forms, instructions, rules, guidelines, and take any other necessary actions needed to implement the amnesty program. And so, this language is very broad. It's more than adequate to give the FTB discretion to determine not to impose penalties in appropriate cases. So, it's not accurate to say that this penalty is strictly mandatory.

And so, I'll skip through some of my comments here.

And so here, the federal control -- the federal definition is either controlling or highly persuasive. A penalty is automatically calculated through electronic means if is proposed by an IRS computer program without human involvement. That comes from the final regulations, and it comes from Walquist versus commissioner. The final regulations say a penalty is automatically calculated through electronic means if an IRS computer program automatically generates a notice to the taxpayer that proposes the penalty. And that comes from the Walquist case and other cases. And so, the FTB does not complain -- does not claim that the relevant notices were generated by computers in this case.

So, in summary, because the post-amnesty penalty is not specifically accepted, it's not calculated automatically by electronic means. The penalty must be approved in writing by a supervisor, and this is an element of the penalty claimed in this case. OTA has jurisdiction to consider it, just like any -- just like the statutory exceptions in Kimberly Clark. We request that the OTA find that the penalty is invalid.

Thank you.

JUDGE LE: Thank you so much for your prevention.

Let me first turn to my panel members to see if they have any questions.

Judge Akin, any questions for Appellant?

JUDGE AKIN: Yes, just a quick follow up. You referenced your Exhibits C through F, I think it was. Which ones were you saying were generated by human versus computer? I just wanted you to repeat that.

MR. CARLSON: So, the only one of those that was not generated by a human, according to the Franchise Tax Board, is Exhibit G. So, the -- so the -- for the rest of the notices, the FTB declined to identify who had prepared the penalties. Exhibit G, the FTB alleged that it was an automated penalty notice but -- so Exhibits C through F were all prepared by human.

JUDGE AKIN: Thank you. That answered my question. Perfect.

JUDGE LE: And turning to Judge Aldrich, any questions?

JUDGE ALDRICH: Yeah. I have a couple of questions. So, in your presentation you made a broad reference to federal authority. Is the federal authority a uniform or are there splits depending upon Circuits?

MR. CARLSON: Yeah, there are Circuits -- Circuit splits on a number of the issues. Sorry. So, there are Circuit splits on a number of the issues. So, for instance, in the Ninth Circuit, there's an issue of when does the penalty have to be approved in writing by a supervisor. And so the -- in the Tax Court, generally the rule outside of the Ninth Circuit is that the penalty has to be approved in writing before the IRS submits its first formal communication of the penalty in writing, and the Ninth Circuit diverges on that. So that's one example.

There's a few different Circuit splits on the relevant issues -- on some of the aspects of the penalty. But in general, the penalties need to be approved in writing, or they're invalidated. There's not a Circuit split on that.

JUDGE ALDRICH: Okay. Thank you.

MR. CARLSON: Thank you.

JUDGE LE: Thank you. And I have a question. You mentioned the Treasury Regulation 301.6551B-1. Sorry. In paragraph F of that regulation, it states that the rules of this section apply to penalties assessed on or after December 23rd, 2024. So, my question is, does this regulation apply to this case?

MR. CARLSON: So, that -- so, that regulation is a restatement of the Tax Court cases. And so it's -- you're correct that it applies to penalties after the regulation became final. But it's a restatement of, you know, the -- the rules set out in Walquist, for example. So, that case describes specifically the issue of whether a penalty is automatically calculated by electronic means. The regulation adopted that portion of -- of the holding in that case. And so really, the relevant part is -- for that regulation is whether a penalty is computed automatically by electronic means. The federal case law is uniform in that issue. And so, the regulation restates it, even though it's applicable only after the regulation became final.

JUDGE LE: That answers my questions. Thank you.

MR. CARLSON: Thank you.

JUDGE LE: Let me now turn to Respondent.

Are you ready for your presentation?

MR. GARCIA-ROSENBLUM: Before -- excuse me. Before Respondent begins, we'd like to request a brief recess.

JUDGE LE: Okay. And how long of a recess do you need?

MR. COUTINHO: Can we get 10 minutes?

JUDGE LE: Ten minutes. Okay. Let's go ahead and take a 10-minute recess.

We are going off the record.

(There is a pause in the proceedings.)

JUDGE LE: Okay. Let's go back on the record.

Tuning to Franchise Tax Board, are you ready for your presentation?

MR. GARCIA-ROSENBLUM: Yes, we are.

JUDGE LE: Okay. You have up to 20 minutes starting at 1:49 p.m. Please proceed.

MR. GARCIA-ROSENBLUM: Thank you.

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PRESENTATION

MR. GARCIA-ROSENBLUM: Good afternoon. My name is Noel Garcia-Rosenblum, and I, along with my co-counsel Bradley Coutinho, represent Respondent Franchise Tax Board in this matter.

This sole issue at appeal today is whether the Office of Tax Appeals has jurisdiction to review the post-amnesty penalty imposed under Revenue & Taxation Code section 19777.5. Based on the legislative purpose and plain language of the section, in conjunction with 20 years of Board of Equalization and Office of Tax Appeals' opinions, the Office of Tax Appeals' jurisdiction is limited to whether Respondent erred in the computation of the post-amnesty penalty. As a preliminary matter, the requirements of Revenue & Taxation Code section 19187(b) do not apply to the post-amnesty penalty. The purpose of Internal Revenue Code section 6751(b)(2) cap (A), which Revenue & Taxation Code section 19187(b)(2) cap (A) is modeled after, it's to prevent IRS agents from threatening unjustified penalties to encourage taxpayers to settle.

Implicit in this legislative history, a taxing agency must have the discretion to impose a penalty for supervisory approval to be required. Accordingly, if supervisory approval is to be required at all, it must be the case that the approval is obtained when the supervisor has the discretion to give or withhold it. When a taxing agency has discretion, it's a crucial factor in determining whether supervisory approval is required for the penalty at issue, under both the Internal Revenue Code section 6751(b) and Revenue & Taxation Code section 19187(b).

In Williams v Commissioner, the United States Tax Court held that the supervisory approval does not apply when a Tax Court imposes a penalty on the taxpayer that makes a frivolous and groundless claims reasoning that the legislative intent of the supervisory approval requirement is to prevent IRS employees from improperly using penalties when they're within their power to determine to course settlements and not intended as a restriction. As relevant to this appeal, the post-amnesty penalty is not imposed during audit where Respondent has the discretion to threaten the penalty to achieve resolutions, but is rather imposed once the underlying tax deficiency on which the penalty rest has been determined with finality, giving Respondent no discretion on whether or not to impose the penalty. Similar to the penalty in Williams, the legislative purpose of the post-amnesty penalty would be frustrated if a non-participating non-compliant taxpayer were to escape the post-amnesty penalty because Respondent did not provide supervisory approval to a penalty that is automatically calculated and imposed.

Furthermore, under Revenue & Taxation Code section 19187(b), supervisory approval is not required if the penalty is calculated through electronic means. In Walquist v Commissioner, the U.S. Tax Court determined that the substantial understatement penalty was automatically calculated through electronic means because the penalty is mathematically calculated, according to a formula derived from the statutory text, is mandatorily imposed unless the statutory exception applies. It cannot be used as a bargaining chip to induce settlement. In this case, the post-amnesty penalty is calculated according to a formula set forth in the statute and is mandatory to impose after a deficiency assessment becomes final; meaning that this penalty cannot be used as a bargaining chip to induce resolution.

Further, Appellant erroneously claims that the post-amnesty penalty was not calculated through electronic means without human involvement. Appellant is unable to point to any conversation, discussion, or any other human involvement he had prior to the post-amnesty penalty being imposed in late 2018 that would reflect that the penalty was used as a bargaining chip to induce him to settle. Therefore, the imposition of the post-amnesty penalty is automatic without allowing for human input or review, and the procedural requirements of Revenue & Taxation Code section 19187 do not apply.

Going back to the central issue at appeal today, Appellant does not contend that the post-amnesty penalty was improperly calculated but instead, attempts to circumvent the statutory limitation by arguing that Respondent did not satisfy the procedural requirements of section 19187(b). As stated previously, this section requires written supervisory approval for certain penalties, but provides exceptions for specific penalties that are automatically calculated through electronic means.

In 2004, the California legislature authorized Respondent to institute an income tax amnesty program for taxable years beginning before January 1st, 2003. This program was enacted with the goal to accelerate the collection of unreported tax liabilities by providing the opportunity to individuals to satisfy unpaid tax balances without penalties, fees, or fear of criminal prosecution. However, eligible taxpayers who chose not to participate were subject to a post-amnesty penalty, under Revenue & Taxation Code section 19777.5, equal to 50 percent of the accrued interest calculated from the original due date to the last date of the amnesty period.

Respondent has no discretion to determine whether the post-amnesty penalty should be imposed when a taxpayer chooses not to participate in the tax-amnesty program. And there are no statutory exceptions for taxpayers who may have acted in good faith or with reasonable cause. Under Revenue & Taxation Code section 19777.5(e), the Office of Tax Appeals review of the post-amnesty penalty is strictly limited to whether Respondent erred in its computation of the penalty. Under Revenue & Taxation Code section 19777.5(d), a taxpayer does not have the right to an administrative protest or appeal of an unpaid post-amnesty penalty, which cuts off Respondent's and the Office of Tax Appeals' discretion to approve or deny the penalty.

Furthermore, the language of the statute restricts a taxpayer's ability to file a claim for refund of a paid post-amnesty penalty on the sole basis of whether the penalty was properly computed. Thus, the language of the statue places clear limitations on how to contest the penalty. Appellant attempts to provide alternative methods to contest the penalty beyond what the California legislature intended. The amnesty penalty and section 19777.5 were enacted in 2004, five years after Revenue & Taxation Code section 19187 was enacted.

If the California legislature was concerned with Respondent's imposition of the post-amnesty penalty, section 19777.5 could have included the requirements of section 19187(b). Instead, the legislative intent demonstrates the intention for a streamline program. This intention was repeatedly held in Board of Equalization and Office of Tax Appeals' opinions wherein both agencies held that their jurisdiction to review the post-amnesty penalty is limited to the computation of the penalty. Therefore, Appellant's argument that the Office of Tax Appeals' jurisdiction should extend beyond the California -- beyond what the California legislature intended is incorrect.

In conclusion, the Office of Tax Appeals' jurisdiction over the post-amnesty penalty is limited to whether the penalty was properly calculated. However, even if this limitation placed by the California legislature were not to apply, the supervisory requirements set forth under section 19187 do not apply to the post-amnesty penalty, as Respondent has no discretion whether to impose the penalty and is automatically calculated through electronic means. Accordingly, Respondent's position should be sustained.

I'm happy to answer any questions the panel may have. Thank you.

JUDGE LE: Thank you for your presentation.

Let me turn to the panel.

Judge Aldrich, any questions?

JUDGE ALDRICH: If you could come back to me. Thank you.

JUDGE LE: Okay. Thank you.

Judge Akin?

JUDGE AKIN: There we go. Got my microphone. No questions. Thank you.

JUDGE ALDRICH: Yeah. So, a part of your argument you were referencing the different effective dates of the statutes. How does that compare with the LCUP penalty that Appellant's counsel was raising? So, I think it was effective September 30th, 2015, for section 19138. He was referencing it in the Kimberly Clark opinion.

MR. COUTINHO: In terms of the five-year difference, the post-amnesty penalty is very unique in the terms of these language provided in 1977.5 subsection -- subdivision (e), in that it basically prohibits anything beyond a claim for refund excluding computation of the penalty. And our position is that if it was to be broader and interpreted for 19187, it would have allowed a carve out or would have specifically allowed for more than just the computation of the penalty in that instance.

JUDGE ALDRICH: Thank you.

JUDGE LE: Thank you. I do have a question. I guess can you address Appellant's argument that there was involvement from FTB employees regarding some of the notices that were sent.

MR. GARCIA-ROSENBLUM: Yes. I believe Appellant references the case with Walquist v. Commissioner. The -- in that opinion, the court concluded that automatically calculated through electronic means meant that the penalty was determined mathematically by a computer software without the involvement of a human IRS examiner. So, the human involvement was related to the calculation of the penalty, that it was done solely by a computer. The opinion does reference that the notice itself was computer generated and sent out, but it was referencing that -- the specific facts of what had happened, not that that was a requirement for the automatically calculated portion.

JUDGE LE: Okay. Thank you.

Let me now turn it back to Appellant for rebuttal, closing statements.

Appellant, are you ready?

MR. CARLSON: Yes, Your Honor. Thank you.

JUDGE LE: Okay. You have up to five minutes.

CLOSING STATEMENT

MR. CARLSON: Some comments here regarding the computation -- the computational issue. Respondent mentions there's been 20 years of BOE and OTA precedent addressing the post-amnesty penalty, but none of these cases address 19187(b). And so, the -- the fact that there's precedent is not helpful if none of those cases have addressed 19187(b).

In terms of the bargaining chip issue, you know, this is a classic case of using a penalty as a bargaining chip. You know, the federal cases talk about the policy rational for requiring written supervisory approval to ensure penalties are not improperly used as a bargaining chip to extract concessions from taxpayers, and this is a perfect example of that. You know, the amnesty letter in -- sent to Appellant in 2004 -- this is Exhibit C. It basically says, "Give up all your rights to dispute 1991 and 1992. Pay us $18.9 million or else you may end up owing $33 million and face stepped-up enforcement efforts," and that sounds pretty threatening to me.

And so, it sounds like it -- but furthermore, those penalties were not unjustified. I mean, they were completely unjustified. Appellant prevailed at the BOE entirely as to tax year 1992. And Appellant --

JUDGE LE: I'm sorry. You reference Exhibit C -- oh. What page are you looking at?

MR. CARLSON: Exhibit C, page 2.

JUDGE LE: Two. Okay. Thank you.

MR. CARLSON: So, Exhibit C, page 2, just has the amounts. So, without amnesty, $33 million. With amnesty, $18.9 million.

Are you able to see it?

JUDGE LE: Okay. Thank you.

MR. CARLSON: Okay. Thank you.

And so, I -- I was saying that, you know, from 1992, Appellant prevailed as to all the issues that were on the table here. And so, you know, FTB is threatening a big penalty, you know, with amnesty for that year, or without amnesty $24.3 million for 1992. Appellant prevailed as to all the issues. And so that penalty, you know, it was not -- it was unjustified.

Furthermore, for 1991, at the time the penalty notice was issued, Appellant prevailed as to all the issues that were being examined. So, residency and the fraud penalty, Appellant prevailed as to both of those issues at the time this notice was issued in 2004. FTB later raised an issue of sourcing in 2007. And so that was years after the penalty -- after the amnesty program had been closed. And so, these were definitely used as bargaining chip. They were definitely perceived that way by Appellant because of -- of the large dollar amounts, and it was completely unjustified.

Regarding discretion, you know, discretion is really -- it's really only relevant when it comes to timing. And so at the federal level we have delayed law opinion. So, that's the Ninth Circuit. It held that 6751(b)(1) requires written supervisory approval before the assessment of the penalty or if earlier, before the relevant supervisor loses discretion whether to approve the penalty assessment. So, you can see in that case really, it's a matter of timing. And so, the penalty had to be approved prior to assessment regardless of discretion. And so 19187(b) doesn't talk about discretion. That's not the test. The test is whether a penalty is automatically calculated by electronic means.

Respondent mentions Williams. So, the Williams case involves a section 6673 opinion for frivolous arguments. That penalty is imposed by the Tax Court. That penalty is not imposed by the IRS in the case where a taxpayer is sanctioned for raising frivolous arguments. And so that is why 6751(b) did not apply in that case. On the Wall case -- on the Walquist case, Respondent mentions it was, you know, 6662 for a substantial understatement. Respondent mentions that this is basically mathematical in nature, but that specific penalty requires written supervisory approval requirement when it's generated by a human. So, in Walquist, the only reason that the supervisory approval requirement did not apply is because a computer generated the penalty notice.

And so, a computer doesn't have a supervisor. It doesn't need to get approval. There's no -- there's no -- it's not going to make a threat to a taxpayer to extract a concession when it brings up a penalty like that. And so that's the reason that Walquist -- that -- that's the reason that the supervisory approval was not required in Walquist. Respondent infers that there should be a repeal by implication, but that's -- it's disfavored, and that's what the federal case law says. That's what the state case law says. We need a strong showing of an intent to repeal. That comes from the Burlington case. And we don't have that here. There's no indication that when the legislature enacted the post-amnesty provisions that it didn't intend supervisory approval to apply.

And I think that's all I have. Thank you, Your Honors.

JUDGE LE: Thank you so much for your closing statements.

Let me turn to the panel one last time to see if there are any final questions by either party.

Judge Akin?

JUDGE AKIN: I have the hardest time with that button. Sorry.

I do have one question for Appellants, and then I would like Respondent Franchise Tax Board to address it after as well.

So, I'm looking at Internal Revenue Code 7491, which is the burden of proof for -- yeah -- in Tax Court for the IRS. And C says that, "Notwithstanding of any other provision of this title, the Secretary shall have the burden of production in any court proceeding with respect to the liability of any individual for any penalty addition to tax or additional amount imposed by this title."

I'm not aware of any similar statute for California purposes. I just wanted to ask Appellants, if under their view, this has any impact on some of the federal court precedent that is being relied upon to say that, you know, the Franchise Tax Board needs to show that the supervisor signature was obtained. Does that --

MR. CARLSON: That's correct. Yeah, I understand it. And so that's -- that's spelled out in the Chai opinion. They talk about 7491. The IRS has generally the burden of production to -- as to penalties and additions to tax. So that was part of the court's analysis in describing the supervisory approval requirement, but it didn't change the court's analysis of whether or not the supervisory approval requirement is an element of the penalty. It relates to the burden of production.

And so, 7491, when there's a penalty on the table, the IRS when it presents its case in Tax Court, it can't simply, you know, allege in pleadings that the penalty applies. It's got to come forward with some evidence to show that there's been negligence, or a substantial understatement of tax, or that a tax return was filed late, or that a tax payment was made late. So, the IRS needs to come forward with some kind of evidence to show -- to meet its burden of production, otherwise the -- the penalty can't be sustained. Once the burden of production has been satisfied, the burden shifts to the taxpayer to raise penalty defenses, like reasonable cause or other defenses. But it doesn't change the fact that supervisory approval is an element of a penalty claim. Just because the FTB doesn't necessarily have a code section that says it has the burden of production, it doesn't mean that this is not an element.

And here, Appellant has done the effort of determining whether there has been supervisory approval of this penalty. And we finally have a concession from the FTB that it was never approved in writing. And so, we don't need a burden of production to require FTB to come forward with that evidence. We've met that evidence, and we've met our burden in this case by establishing that element.

JUDGE AKIN: Thank you.

Franchise Tax Board, I'd like you to respond as well if you had any commentary you'd like to address on that question.

MR. COUTINHO: Franchise Tax Board doesn't have a particular opinion on that particular. We're happy to provide additional briefing regarding that particular code section. But we will note, contrary to Appellants' assertion regarding 19187 that every penalty requires supervisory approval, their specific carve outs as noted in(b)(1), (b)(2), (b)(3). And specifically, in the language of 19187. The language talks about the initial determination. And to that point, there's a discretion element that even Appellant kind of concedes with the idea that a computer doesn't have discretion. Discretion is an important part of the determination under 19187 and whether supervisor approval is necessary.

Thank you.

JUDGE AKIN: Understood. And that answers my question. So, thank you.

JUDGE LE: Thank you.

Turning to Judge Aldrich, any questions?

JUDGE ALDRICH: No further questions.

JUDGE LE: Okay. And for me I also don't have any further questions. So, if there's nothing else, that will conclude our hearing.

Thank you, everyone, for coming in today.

This case is submitted on April 21st, 2026. The judges will meet and decide your case later on, and we will send the parties a written opinion of our decision within 100 days.

Today's hearing in the Appeal of Hyatt is now concluded, and we are off the record.

Thank you.

(Proceedings concluded at 2:10 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 14th day of May, 2026.

____
ERNALYN M. ALONZO
HEARING REPORTER