OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

In the Matter of the Appeal of: **SHARON MITCHELL**	OTA Case No. 18011715

OPINION ON PETITION FOR REHEARING

Representing the Parties:

For Appellant:	Christina Weed, Esq. Lisa Mendez, Esq.
For Respondent:	David Gemmingen, Tax Counsel IV Ciro Immordino, Tax Counsel IV Michael Cornez, Tax Counsel V

T. STANLEY, Administrative Law Judge: On August 2, 2018, we issued an opinion reversing Franchise Tax Board's (FTB) action proposing an assessment of $60,209 of additional tax, for the 2007 tax year, resulting from the dissolution of a partnership, Con-Med, in which appellant held a 10 percent interest. Appellant Sharon Mitchell argued on appeal that tax on her gain should be deferred because the sale of the sole asset of the partnership, a parcel of commercial real estate (the property), had been structured by the partnership to allow appellant, and other partners choosing to do so, to convert their partnership interests to tenant-in-common (TIC) interests and then exchange those interests for like-kind property under Internal Revenue Code (IRC) section 1031. FTB argued on appeal that appellant had not completed a valid 1031 exchange, primarily because she was not the seller – the partnership was – and even if she had been a seller, the transaction violated the rules against anticipatory assignment of income. The majority agreed with the appellant with Judge A. Rosas dissenting. Pursuant to Revenue and Taxation Code (R&TC) section 19048, FTB petitioned for a rehearing.

Office of Tax Appeals (OTA) may grant a rehearing where one of the following grounds is met and materially affects the substantial rights of the party seeking a rehearing: (1) an irregularity in the proceedings that prevented the fair consideration of the appeal; (2) an accident

or surprise that occurred, which ordinary caution could not have prevented; (3) newly discovered, relevant evidence, which the filing party could not have reasonably discovered and provided prior to issuance of the written opinion; (4) insufficient evidence to justify the written opinion or the opinion is contrary to law; or (5) an error in law that occurred during the proceedings. (Cal. Code Regs., tit. 18, § (Regulation or Reg.) 30604; *Appeal of Do*, 2018-OTA-002P; *Appeal of Wilson Development, Inc.* (94-SBE-007) 1994 WL 580654.) We conclude that the grounds relied upon in the petition do not constitute good cause for a new hearing.

Specifically, FTB alleges its rights were materially affected by the following:

- The lead judge prematurely terminated FTB's closing argument, which was an irregularity in the proceeding that prevented FTB from having a fair hearing;
- There is insufficient evidence to justify the opinion[1] or the opinion is contrary to law in that it contains factual findings and statements that are supported exclusively by inadmissible hearsay evidence or that are contrary to California law;
- There is insufficient evidence to justify the opinion or the opinion is contrary to law in that the most reliable and probative evidence proves the seller of the property was the partnership;
- The opinion contains an error in law as it does not apply the U.S. Supreme Court's analysis in *Commissioner of Internal Revenue v. Court Holding Co.* (1945) 324 U.S. 331 (*Court Holding*) to establish who is the seller for tax purposes, an analysis which was followed by the Board of Equalization (BOE) in its precedential decision in *Appeal of Brookfield Manor, Inc. et al.* (89-SBE-002) 1989 WL 37900; and,
- The opinion contains an error in law as it erroneously rejected FTB's anticipatory assignment of income argument.

We address each of these contentions below.

1. Irregularity in the Proceedings

An irregularity in the proceedings is defined as "any departure . . . from the due and orderly method of disposition of any action by which the substantial rights of a party have been materially affected." (*Appeal of Graham and Smith*, 2018-OTA-154P.) The granting or denial

[1] This and later references to the "opinion" are to the majority opinion.

of a new hearing on such basis is largely in the discretion of the presiding officer. (*Loggie v. Interstate Transit Co.* (1930) 108 Cal.App. 165, 171.) Courts have defined an irregularity in the proceedings as "an overt act [. . .] violative of the right to a fair and impartial trial, amounting to misconduct." (*Gray v. Robinson* (1939) 33 Cal.App.2d 177, 182.) Courts have also required, in addition to identifying such an irregularity, that the petitioning party show they were ignorant of the facts constituting the irregularity prior to the decision, "since it is settled that a party may not remain quiet, taking his chances upon a favorable verdict, and, after a verdict against him, raise a point of which he knew and could have raised during the progress of the [proceedings]." (*Id.* at p. 183.)

FTB contends that the panel prematurely terminated FTB's closing argument and therefore prevented it from having a fair consideration of its case. Following approximately one hour of FTB's closing argument, the lead judge interrupted and stated, "Can I just point out that you guys have been closing for almost an hour? And so, I'd appreciate if you could make final points and try to wrap this up." FTB contends that it had not been making its closing argument for an hour; rather, it spent most of that time addressing questions previously posed by the panel. It asserts that its rights were materially affected because it was not allowed to finish its prepared remarks. Specifically, FTB contends that it was foreclosed from addressing Con-Med's tax documents (K-1s).

The panel's imposition of reasonable time constraints on the parties' closing arguments was consistent with an orderly hearing process. FTB was free to present its closing argument in the manner it wished. The only evidence mentioned in the petition for rehearing (PFR) is the partnership's Forms K-1, which "did not increase the non-redeeming partners' interests at the end of its 2007 taxable year, demonstrating that Con-Med did not, for tax purposes, respect the redemption of appellant and her mother." The record reflects that FTB chose two attorneys to present its closing argument, each addressing different topics, as well as to address panel questions, for approximately one hour, uninterrupted. FTB's argument covers approximately 36 pages of transcript. By comparison, appellant's opening and rebuttal arguments cover approximately 18 pages of transcript.[2] Furthermore, FTB's substantive rights were not materially affected by its failure to explain the significance of certain documents. The parties

[2] Appellant had the primary burden of proof. Typically, OTA allows the party with the burden of proof additional time to present a rebuttal to the agency's argument.

fully briefed the issues, and the documents were admitted into the record. We find nothing in the record that can be reasonably construed as notice to the panel that there was an important issue that required additional argument. OTA judges have the inherent authority to take any action deemed necessary for the orderly and fair adjudication of disputes within OTA's jurisdiction.[3] We thus find that the lead judge's actions were entirely within that authority and were not irregularities that warrant a rehearing.

2. Sufficiency of the Evidence to Justify the Decision

A rehearing should not be granted on the grounds of insufficiency of the evidence unless, after weighing the evidence, we are convinced from the entire record, including reasonable inferences therefrom, that we should have reached different conclusions. (Cal. Code Civ. Proc., § 657.)[4] In addition, insufficiency of the evidence as a ground for a rehearing means the level of insufficiency that causes a trier of fact, when weighing conflicting evidence, to thereafter conclude that facts in support of the decision weigh less than those which are in opposition. (*Bray v. Rosen* (1959) 167 Cal.App.2d 680, 683.)

FTB contends that the opinion relies on factual findings and statements that are supported exclusively by inadmissible hearsay evidence, and therefore FTB's rights were materially affected because there is insufficient evidence to justify the majority opinion. Those key findings and statements in the opinion include the following:

- Con-Med's representative negotiated the sale or exchange of the property on behalf of its 17 partners,
- the plan by some partners to do 1031 exchanges was known to all from the beginning,
- everyone knew that the transfer of the property may involve procedures and documents to allow the exchanges to occur,[5]

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[3] This authority is now codified. (Cal. Code Regs., tit. 18, § 30213(j).)

[4] In *Appeal of Wilson Development, Inc., supra*, the BOE largely adopted the grounds for granting a rehearing, including the ground of an insufficiency of evidence to justify the decision, from Code of Civil Procedure section 657, which sets forth the grounds for a new trial in a California trial court.

[5] FTB also mentions our finding that, as early as 1990, Caroline Mitchell and PTLA were discussing a 1031 exchange as a choice for the Con-Med partners. Exhibit 34 is the only evidence that tends to prove that Caroline Mitchell and PTLA were discussing a 1031 exchange as a choice for the Con-Med partners as early as 1990, and in that regard, FTB's position is well taken. However, the fact is not required to support the ultimate disposition.

- only Con-Med's name appears on counteroffers, which reflects the state of the title to the property at the time.
- Con-Med recognized by 2005 that it would probably have to sell the property and that Con-Med would need a plan to accommodate partners who wanted to continue their investment in like-kind property, as well as those who wanted to cash out their investment.[6]
- Milner advised other Con-Med partners that there had been inquiries from at least one partner regarding the procedure for structuring any sale to facilitate a valid 1031 exchange.[7]
- A number of the partners wanted to have their share of the sale proceeds deposited into an "exchange account; and attorney Goodman had previously indicated that "exchanging some partners into a new partnership while 'cashing out' others would be difficult."[8]
- Milner accepted the last counteroffer, and explained there were several contingencies, including approval by the Con-Med partners by March 21, 2007; the escrow close date could be extended to facilitate a 1031 exchange; and that, if Con-Med's accountants approved, Milner would adopt a second amendment to the partnership agreement that would require dissolution of the partnership and distribution to the partners of undivided interests in the Property before the close of escrow.[9]

As an administrative agency, "OTA conducts hearings and proceedings in accordance with the Administrative Procedure Act using hearing procedures that are accessible to all representatives, including non-lawyers and taxpayers who are representing themselves." (Cal. Code Regs., tit. 18, § 30216(c).)[10] OTA may admit any relevant evidence, including hearsay evidence, provided that "it is the sort of evidence on which responsible persons are accustomed to rely in the conduct of serious affairs, regardless of the existence of any common law or statutory rule which might make improper the admission of the evidence over objection in civil

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[6] Findings of Fact number 5.

[7] Findings of Fact number 6.

[8] Findings of Fact number 7.

[9] Findings of Fact number 12.

[10] Contained in Regulation section 30708 of the emergency regulations in effect at the time of the hearing.

actions." (Cal. Gov. Code, § 11513(c).)[11] A sworn affidavit may be introduced in evidence in an administrative proceeding, "but shall be given only the same effect as other hearsay evidence." (Cal. Gov. Code, § 11514.) "Hearsay evidence may be used for the purpose of supplementing or explaining other evidence but over timely objection shall not be sufficient in itself to support a finding." (Cal. Gov. Code, § 11513(d); *Steen v. Bd. of Civil Service Commissioners* (1945) 26 Cal.2d 716, 727.)

In this hearing, the lead judge admitted some evidence, notably appellant's exhibits 34 (identified as "Beler letter") and 46 (the "Milner declaration") over FTB's timely objection but subject to the limitation that the evidence would not be considered sufficient alone to support a finding of fact.[12] All of the other evidence that the panel relied upon was admitted without objection or limitation.

Milner's 2005 email to the Con-Med partners (exhibit 3) shows that one or more partners had asked him questions about a possible 1031 exchange. There was no objection to the admission of this evidence. The email contains a recommendation to the partners to talk to their tax advisors if they were interested in doing a like-kind exchange, and it states that he will "make sure that our lawyer (attorney Goodman) has set up the mechanism correctly for any partners who wish to do a 1031 exchange of property." This is a clear statement by the managing partner to represent the interests of the partners who wanted to do a like-kind exchange, and the statement occurred before he (and possibly others) negotiated the sales agreement.

Milner's July 27, 2005 email to attorney Goodman (exhibit 38) mentions that some partners were interested in completing like-kind exchanges and states that Milner was not sure if this needed to be mentioned in the offer. FTB did not object to the admission of this evidence. The email goes on to request more information about how difficult it would be to structure the sales to allow some partners to exchange and others to cash out. This evidence shows that Milner intended to negotiate the exchange option for appellant and her mother, if feasible.

Milner's January 5, 2007 email to the partners (exhibit 44) attaches the initial offer and refers to a prior telephone conference during which the partners discussed the pros and cons of PTLA's opening offer to buy the property for $6 million. There was no objection to the

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[11] Under the emergency regulations in existence at the time of the hearing, OTA was subject to California Government Code section 11513. Effective January 1, 2019, that section no longer applies to proceedings before OTA. (Cal. Code Regs., tit. 18, § 30216(d).)

[12] In this instance, a timely objection is one raised before submission of the case.

admission of this evidence. The first and fifth bullet items listed in the email as being among the items discussed are the following, in order:

> Since some partners wish to do an exchange for tax purposes, we would have to break up the partnership into tenants-in-common to do so. If we did this, could 1 partner "foul the deal" by changing their minds during escrow? (Unlikely but a risk.)
>
> I talked with our lawyer afterwards who said we would merely put the "Dissolution of partnership" contingent upon close of escrow. Those partners who wish to do an exchange (currently 3 that I know of) would pick up/split the ~ $2,000 legal fees.
>
> ***
>
> Capital gains taxes are expected to rise over the next couple of years. This was mentioned as a reason for taking the current offer rather than waiting.

This shows that all the partners, including appellant and her mother, were discussing that some wanted to do an exchange and others were concerned that those few might be able to prevent the sale and keep the others from cashing out. The email goes on to note that, with about 80 percent voting in favor of the offer during the telephone conference, Milner instructed attorney Goodman to "update the offer." The majority views this as further evidence that Milner was representing the interests of all the partners in the negotiations. The fact that the partnership was dissolving is further evidence that the diverse plans of the individual partners were likely his main concern.

Milner's March 7, 2007 correspondence (exhibit 36) informed the Con-Med partners that Milner signed the final counter offer. There was no objection to the admission of this evidence, which states, in part, that close of escrow was set for August 31, 2007, but might be extended up to an additional 60 days if either party needed additional time to complete a tax deferred exchange under IRC section 1031. The correspondence also discusses a possible amendment to the partnership agreement to facilitate the exchanges. The majority viewed that as further evidence of Milner's successful efforts to negotiate an exchange option for at least two of the Con-Med partners, despite the fact that close of escrow could be delayed to allow sufficient time to accommodate those partners, and the absence of a clear plan regarding how the exchanges were to be executed.

The evidence discussed above is sufficient to support our finding that Con-Med's representative negotiated the sale *or exchange* of the property on behalf the partnership and its

17 partners so that the partners could determine whether they wished to become tenants in common and exchange their interests rather than cashing out after the partnership terminated. The finding is also supported by the agreement, which refers to the exchange option, and the Milner declaration, which specifically states, among other things, that the transaction was arranged on behalf of the partnership and Sharon and Caroline Mitchell. Furthermore, we find unpersuasive FTB's argument that the parties to the agreement understood that the exchange option could be exercised by the partnership, not by the partners. We found it more likely that PTLA was aware from at least near the beginning of negotiations that some Con-Med partners planned to exchange their partnership shares for TIC shares and then exchange those shares for like-kind property, and that PTLA and Milner included that option for those partners. Finally, the opinion recognizes the distinction between appellant's ownership of her 10 percent partnership interest, which was not a direct interest in the property, and appellant's 10 percent TIC interest, which was a direct interest in the property, and we did not find otherwise, though the reference to appellant continuously holding an "interest" in the property could have been stated more clearly.

We find there is sufficient evidence in the record to support findings that: Milner negotiated the sale on behalf of the partners, including appellant; Milner specifically negotiated the exchange option for appellant and her mother (and any other partners who could have chosen the option); and, while the specific details of how the exchange options would be exercised was not clear at the outset, the Con-Med partners and PTLA were aware no later than early in the negotiations that some Con-Med partners planned to exchange their partnership shares for TIC shares and then exchange those shares for like-kind property, which might require the redemption of the partnership shares for equivalent TIC shares. Thus, there is substantial support in the record to justify the opinion.

3. Contrary to Law

The question of whether the decision is contrary to law (or against law) is not one which involves a weighing of the evidence, but instead requires a finding that the decision is "unsupported by any substantial evidence." (*Sanchez-Corea v. Bank of Am.* (1985) 38 Cal. 3d 892, 906.) This requires a review of the decision to "indulg[e] in all legitimate and reasonable inferences" to uphold the decision. (*Id.* at p. 907.) The question with respect to the petition for rehearing is not over the quality or nature of the reasoning behind the decision, but whether the

decision can or cannot be valid according to the law. (*Appeal of NASSCO Holdings, Inc.* (2010-SBE-001) 2010 WL 5626976.)

FTB contends that the opinion is contrary to law because the majority opinion failed to apply the judicial doctrine of substance-over-form when analyzing the exchange requirement of IRC section 1031. In essence, FTB argues that its action should have been sustained as a matter of law. Specifically, FTB claims that the opinion erred by not applying the substance-over-form doctrine.[13] It claims the opinion was instead reasoned on the application of the "step-transaction doctrine." In addition, FTB asserts that the panel erred in discussing and determining whether appellant had met the "holding" requirement of a 1031 exchange. (See IRC, § 1031(a)(1) [gain or loss is deferred on the exchange of real property if it is held for productive use in a trade or business or for investment].) However, because FTB did not stipulate that appellant had met any requirement necessary to effectuate a valid 1031 exchange, all requirements had to be addressed in the opinion, including the holding requirement, thus there was no error in that respect.

There may have been some conflation in the opinion of the substance-over-form and the step-transaction analyses. FTB, which argued both theories, describing them as "two guiding principles" followed by our predecessor, the BOE, also may have comingled the two. (See, e.g., FTB's Opening Brief, p. 4, ll. 2-25.) It is not surprising given their common purpose: to honor substance over form, viewing a transaction as a whole. In fact, the step-transaction doctrine is a subset, or corollary, of the substance-over-form doctrine which defines the incidence of taxation, depending on the substance rather than the form of a transaction. (*Security Industrial Ins. Co. v. United States* (5th Cir. 1983) 702 F.2d 1234, 1444.) Collapsing steps in a transaction is one of the mechanisms courts have used to determine the substance of a transaction for tax purposes. (See *Commissioner v. Court Holding Co.* (1945) 324 U.S. 331 (*Court Holding*); *True v. United States* (10th Cir. 1999) 190 F.3d 1165, 1176 n.11; *Tandy Corp. v. Commissioner* (1989) 92 T.C. 1165, 1171.)

FTB's argument in its petition for rehearing focuses primarily on its view that the opinion did not apply the substance-over-form doctrine set forth in *Court Holding*. However, we did not ignore *Court Holding* or its progeny. Instead, we distinguished them on the basis that the facts of this transaction are materially different. In this appeal, we weighed the evidence and found that appellant met all requirements for a valid 1031 exchange and that there was no effort to

[13] FTB refers to a "seller-in-substance doctrine," but that appears to be a doctrine of its own creation.

disguise the transaction or its various components by "mere formalisms." (See *Court Holding, supra*, 324 U.S. 331, at p. 334.) Moreover, FTB has offered no other way that appellant could have structured the transaction in a manner other than the way appellant chose. (See *Magneson v. Commissioner* (1985) 753 F.2d 1490.) Accordingly, we did not err by discussing and rejecting use of the step-transaction doctrine to determine whether the substance was reflected in the form chosen.

FTB has not persuaded us that we incorrectly applied the law, by making the same arguments now that it made prior to issuance of the opinion. We made findings based on the weight of the evidence and rejected FTB's arguments to the contrary. We specifically found that appellant sold 10 percent of the property to the buyers. We found that the parties to the transaction, including appellant, did what they thought was required to accomplish their diverse objectives; appellant's objective being the continued investment in real property. We found then, as we still find, that appellant followed the plan laid out by the Con-Med managing partner and the lawyer to navigate the still largely uncharted and obviously treacherous path from owning real property through a partnership interest to direct ownership of a property that successfully results in a valid 1031 exchange. The evidence does not establish that appellant, or anyone else, attempted to disguise these related transactions by mere formalisms.

Since before 1984, when section 1031 was amended to specifically prohibit the exchange of partnership interests, there has been no clear path to guide partners who wish to continue their investment in like-kind property. The situation is further complicated when fewer than all partners want to remain invested in like-kind property. As we stated in the opinion, appellant did not engage in an improper tax avoidance scheme. The exchange was not a sham. The parties engaged in a series of reasonable, necessary, and integrated transactions to accomplish a 1031 exchange. There was no last-minute decision to change the parties to the sale.

We find that the opinion is not contrary to law nor was there an error in law that occurred during the proceedings, and that FTB's substantial rights were not materially affected.

FTB, lastly, asserted that we erred by rejecting FTB's anticipatory assignment of income argument. We held that appellant's interest in a pass-through entity had the same economic consequences as holding a TIC with the partnership. The transfer did not shift income from one

individual to others as was done in FTB's cited case, *Salvatore v. Commissioner* (1970) T.C. 7 Memo 1970-30. The distinction is not contrary to law.

We conclude FTB has not shown good cause for a new hearing and deny its petition.

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Teresa A. Stanley
Administrative Law Judge

I concur:

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Michael F. Geary
Administrative Law Judge

A. ROSAS, Concurring and Dissenting, in part:

At the outset, let me say that I concur with the first section from the majority's Opinion on Petition for Rehearing (Opinion on PFR), but I respectfully disagree with the conclusions reached in the second and third sections of the Opinion on PFR.

1. Irregularity in the Proceedings

The April 24, 2018 oral hearing did *not* constitute "an irregularity in the proceedings by which the party was prevented from having a fair consideration of its appeal." (Cal. Code Regs., tit. 18, § 30604(a); *Appeal of Wilson Development, Inc.* (94-SBE-007) 1994 WL 580654; *Appeal of Do*, 2018-OTA-002P.) Respondent Franchise Tax Board argues that there was an irregularity in the proceedings because the panel "prematurely terminated" respondent's closing argument and that this purportedly prevented respondent from having a fair consideration of its case. Respondent's argument lacks merit, and it does not warrant any further discussion beyond the discussion that the Opinion on PFR has already devoted to it.

However, I conclude that respondent has shown good cause for a new hearing under two separate grounds: first of all, there is insufficient evidence to justify the majority's August 2, 2018 Opinion (Opinion); and secondly, that Opinion is contrary to law. (Cal. Code Regs., tit. 18, § 30604(d); *Appeal of Wilson Development, Inc.*, *supra*; *Appeal of Do*, *supra*.)

2. Sufficiency of the Evidence to Justify the Decision

There is insufficient evidence to justify the August 2, 2018 Opinion. As applicable to administrative bodies, a rehearing should not be granted on the grounds of insufficiency of the evidence unless, after weighing the evidence, one is convinced from the entire record, including reasonable inferences therefrom, that the panel clearly should have reached a different decision. (Cal. Code Civ. Proc., § 657.) Here, in analyzing whether there is insufficient evidence to justify the majority Opinion, one must review whether there is insufficient evidence to support the majority Opinion's determination that appellant Sharon Mitchell satisfied both the exchange requirement and the holding requirement.[1]

I agree with respondent's contentions that the majority based its factual findings and statements exclusively on inadmissible hearsay evidence, and, therefore, this materially affected

[1] The "like-kind" requirement, under IRC section 1031, is not at issue.

respondent's rights because there is insufficient evidence to justify the majority Opinion. Granted, during the April 24, 2018 oral hearing, the Office of Tax Appeals (OTA) was subject to the Emergency Regulations on Rules for Tax Appeals and, under these emergency regulations, OTA was able to admit any relevant evidence, including hearsay evidence, provided that "it is the sort of evidence on which responsible persons are accustomed to rely in the conduct of serious affairs, regardless of the existence of any common law or statutory rule which might make improper the admission of the evidence over objection in civil actions." (Cal. Gov. Code, § 11513(c).)[2]

However, notwithstanding Government Code section 11513(c)'s broad rule of evidence admissibility, the California "residuum rule" requires that an administrative law judge's findings be supported by at least *some evidence other than hearsay.* (See *The Utility Reform Network v. Public Utilities Com.* (2014) 223 Cal.App.4th 945, 960-61.) In California, administrative decisions adhere to the "'residuum rule,' under which the substantial evidence supporting an agency's decision must consist of at least 'a residuum of legally admissible evidence.'" (*Ibid.*, internal citation omitted.) Thus, over timely objection, hearsay evidence "shall not be sufficient in itself to support a finding unless it would be admissible over objection in civil actions." (Cal. Gov. Code, § 11513(d); *Lake v. Reed* (1997) 16 Cal.4th 448, 458, discussing former Cal. Gov. Code, § 11513(c).)

Hearsay evidence in administrative adjudicatory proceedings is usually referred to as "administrative hearsay," meaning that it is admissible to supplement or explain other evidence, but not itself sufficient to support a finding. Thus, there must be "substantial evidence" to support the majority Opinion, "and hearsay, unless specially permitted by statute, is not competent evidence" to support the majority's rulings. (See *Walker v. City of San Gabriel* (1942) 20 Cal.2d 879, 881.) Furthermore, as the California Supreme Court stated: "Except in those instances recognized by statute where the reliability of hearsay is established, hearsay evidence alone 'is insufficient to satisfy the requirement of due process of law, and mere uncorroborated hearsay does not constitute substantial evidence.'" (*In re Lucero L.* (2000) 22 Cal.4th 1227, 1245, quoting *Gregory v. State Board of Control* (1999) 73 Cal.App.4th 584, 597.) Here, the evidentiary record lacks any substantial evidence to support the majority Opinion.

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[2] Effective January 1, 2019, California Government Code section 11513 no longer applies to proceedings before OTA. (Cal. Code Regs., tit. 18, § 30216(d).)

Thus, the Opinion did not follow the California "residuum rule" and relied on inadmissible hearsay to support many of its findings. As I pointed out in the August 2, 2018 Dissent, the majority Opinion based many of its findings on inadmissible evidence and speculation. Therefore, I conclude that there is insufficient evidence to justify the majority Opinion, and I find there is good cause for a new hearing on this ground.

3. Contrary to Law

The August 2, 2018 Opinion is contrary to law. After considering the authorities in the August 2, 2018 Dissent, "considering the evidence in the light most favorable to the prevailing party, [. . .] and indulging in all legitimate and reasonable inferences" to uphold the August 2, 2018 Opinion, in examining the record I cannot find the existence of "substantial evidence" to support the majority Opinion. (*Sanchez-Corea v. Bank of Am.* (1985) 38 Cal.3d 892, 907.) Appellant had the burden of proving error in respondent's application of the substance-over-form doctrine, the application of which led respondent to determine that appellant did not satisfy the exchange requirement in her attempted Internal Revenue Code (IRC) section 1031, drop-and-swap exchange. (*Todd v. McColgan* (1949) 89 Cal.App.2d 509; *Appeal of Myers* (2001-SBE-001) 2001 WL 37126924.) The majority Opinion fails to evaluate the record through the legal framework established for drop-and-swap transactions, including *Commissioner v. Court Holding Co.* (1945) 324 U.S. 331; *U.S. v. Cumberland Public Service Co.* (1950) 338 U.S. 451; *Appeals of Brookfield Manor, Inc. et al.*(89-SBE-002) 1989 WL 37900; *Chase v. Commissioner* (1989) 92 T.C. 874; and *Bolker v. Commissioner* (1983) 81 T.C. 782.

Instead, I believe the majority Opinion erroneously conflates the analysis of the holding requirement with that of the exchange requirement, relying on authorities that focus on the holding requirement in order to determine whether appellant satisfied the exchange requirement of IRC section 1031. In doing so, the Opinion cannot be valid according to the law. (*Appeal of NASSCO Holdings, Inc.* (2010-SBE-001) 2010 WL 5626976.)

Therefore, because I conclude that the majority Opinion is contrary to law and that their disposition materially affected respondent's rights, I find there is good cause for a new hearing based on this ground as well.

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Alberto T. Rosas
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Alberto T. Rosas
Administrative Law Judge

Date Issued: 1/28/2020