

Memorandum

To: Honorable John Chiang, Chair
Honorable Claude Parrish, Vice Chairman
Ms. Betty T. Yee, Acting Board Member
Honorable Bill Leonard
Honorable Steve Westly

Date: May 5, 2006

From: Kristine Cazadd 
Chief Counsel

Subject: **Board Meeting – May 17, 2006**
Chief Counsel Matters – Item J2

Concept Approval of Chapter 4, *Appeals from Actions of the Franchise Tax Board*, New Rules of Practice¹

I. Summary and Recommendation

Staff presented the first draft of Chapter 4, *Appeals from Actions of the Franchise Tax Board*, to the Board and the interested parties at the September 28, 2005, Board meeting, and then held an interested parties meeting on December 14, 2005. Based upon comments from the interested parties, staff revised Chapter 4 and issued a second draft, which was discussed at a second interest parties meeting on March 15, 2006. Based on the valuable comments from interested parties at each meeting, staff has fully developed the main concepts for Chapter 4, and hereby requests Board approval before finalizing the language. Staff requests your approval of the main concepts embodied in Chapter 4 as set forth below, and as described in detail in the remainder of this memorandum:

- Allow for three different briefing schedules: A general default briefing schedule, which will be applicable to the majority of appeals; an elective, simplified briefing schedule, which limits the Franchise Tax Board (FTB) to a single response; and a briefing schedule for innocent spouse appeals, which permits the non-appealing spouse to materially participate in the briefing process;
- Establish new discretionary pre-hearing conferences, which may be requested by the appellant, the FTB, or a Board Member; and

¹ Staff is in the process of renaming the rules per direction provided by the Board at the April 18, 2006, Board meeting.

- Set forth general procedures for issuing Summary Decisions, Letter Decisions, and Formal Opinions, which permit dissenting and concurring Board Members to adopt their own rationale for a Formal Opinion.
- Clarify procedures for imposing frivolous appeal penalties and procedures for grant/denying/holding rehearings.

II. General Concepts Contained in Chapter 4, Appeals from Actions of the Franchise Tax Board

Chapter 4 generally follows the Board's current procedures and policies with regard to appeals from actions of the FTB and will incorporate the e-filing language the Board approved in concept at the April 18, 2006, Board meeting. However, staff considered suggestions for several modifications to the Board's current procedures, and has decided to recommend a few changes to the Board's current procedures and policies, which are discussed in detail below.

A. Chapter 4's Procedures for Resolving Jurisdictional Issues

Appeals from the FTB sometimes raise issues as to the Board's jurisdiction. In such cases, the Board's current policy is to:

- Reject appeals over which the Board clearly lacks jurisdiction. Those include appeals filed well after the statutory filing deadline, appeals that take issue with the behavior of FTB employees but do not challenge the amount of a tax liability, or appeals of liabilities that have no statutory appeal right;
- Accept appeals over which the Board clearly has jurisdiction;
- Accept appeals that raise a genuine issue as to the Board jurisdiction. Those include, for example, appeals received near the statutory filing deadline with a smudged postmark, or appeals on claims for refund that may or may not have been perfected. When the Board accepts an appeal that raises a genuine jurisdictional issue, the matter of jurisdiction is considered "at issue" in the appeal and is decided by the Board like any other matter at issue in the appeal.

During the interested parties process, the FTB suggested that the Board bifurcate appeals that raise a genuine issue as to the Board's jurisdiction so that the jurisdictional issues can be briefed and decided by the Board before the FTB is required to brief and argue the substantive issues raised in such appeals. Staff considered this suggestion, but did not incorporate it into Chapter 4 because the law does not require the Board to bifurcate jurisdictional issues, bifurcation would be administratively inefficient for the Board and appellants, and bifurcation would be difficult to achieve in practice.

Bifurcation would be inefficient for the Board and appellants because it would require appellants to brief their jurisdictional issues, then possibly participate in an appeals conference and attend a Board hearing solely on those jurisdictional issues. If the Board decided that it had jurisdiction to hear the appellants' appeals, the appellants would then start the entire process anew in order to argue the substantive issues in their appeals. Bifurcation would be difficult to achieve in practice because it would also require the Board to ignore the substantive issues in an appeal while it considered the jurisdictional issues at the first hearing, which would impose a substantial limitation on the Board's traditional discretion to decide appeals.

Although staff did not incorporate the FTB's suggestion for bifurcation, staff did try to address the FTB's jurisdictional concerns by revising and clarifying the procedures under which appeals are reviewed and either accepted or rejected. Under Chapter 4's proposed procedure, the Chief of Board Proceedings will accept appeals over which the Board clearly has jurisdiction, reject appeals over which the Board clearly lacks jurisdiction, and refer appeals to the Chief Counsel where jurisdiction is unclear or requires further investigation. When an appeal is referred to the Chief Counsel, the Chief Counsel will review the appeal, obtain any additional information that is relevant to determining jurisdiction, and make a determination. If the Chief Counsel determines that the Board lacks jurisdiction, the Chief of Board Proceedings will reject the appeal. If the Chief Counsel determines that the Board has jurisdiction or the appeal raises a genuine issue regarding jurisdiction, the appeal will be accepted and the briefing process will start. In appeals where there is a genuine issue regarding jurisdiction, the parties will be expected to brief the jurisdictional issue for the Board's decision, just like any other substantive issue raised in the appeal.

Staff believes that Chapter 4's proposed procedure, which is only a minor departure from current procedures, strikes an appropriate balance between the efficient use of BOE and FTB resources and providing taxpayers with a clear and simple process.

B. Chapter 4's Procedures for Perfecting Incomplete Appeals

When appellants file timely but incomplete appeals, the Board's current *Rules of Practice* grant an additional 90 days to perfect the appeals. Chapter 4 proposes to continue the Board's policy of granting appellants 90 days to perfect timely filed appeals. Chapter 4 also would provide more guidance regarding the information needed to perfect the appeal and would give the Chief of Board Proceedings authority to grant extensions of time with the consent of all the parties or in cases of extreme hardship. Finally, Chapter 4 would clarify that an appeal must be perfected before the briefing process may begin and, if the taxpayer fails to provide the information needed to perfect the appeal, the appeal will be dismissed.

C. Chapter 4's Three (3) Different Briefing Schedules

The Board's current *Rules of Practice* contain a single briefing schedule that is applicable to all appeals from the FTB. After receiving considerable input from interested parties, as well as

observing the operation of the single briefing schedule in actual practice, staff has determined that appeals could be processed more fairly and efficiently if there were different briefing schedules applicable to different kinds of appeals. Accordingly, Chapter 4 proposes three different briefing schedules: a general briefing schedule that would be applicable to most appeals by default, a simplified briefing schedule that qualified appellants could elect to use, and a more detailed briefing schedule that would apply to innocent spouse appeals (which are complex because they involve two appellants with adverse interests).

General, Default Briefing Schedule

Chapter 4's general briefing schedule is very similar to the briefing schedule contained in the current *Rules of Practice* and would apply to most appeals by default. The perfected appeal is considered the appellant's opening brief. Within 90 days of the acknowledgement of the perfected appeal, the FTB may file its opening brief. After the FTB's opening brief is acknowledged, the appellant has 30 days within which to file a reply brief addressing areas of disagreement with the FTB's opening brief. If the appellant files a reply brief, the FTB will be given 15 days from the acknowledgement of the appellant's reply brief to request permission to file its own reply brief. If the Chief Counsel determines that additional briefing is necessary, the Chief Counsel may grant the FTB 30 days to file a reply brief addressing areas of disagreement with the appellant's reply brief. In order to ensure fair and consistent administration of that provision, the proposed regulation sets forth a list of examples for determining when additional briefing is necessary. If the FTB files a reply brief, the appellant will automatically be granted 30 days within which to file a supplemental brief addressing areas of disagreement with the FTB's reply brief.

Elective, Simplified Briefing Schedule

Chapter 4 proposes an elective, simplified briefing schedule that would apply to franchise and income tax appeals where the amount at issue does not exceed \$15,000, as well as all appeals filed pursuant to the Homeowners and Renters Property Tax Assistance Law. However, the simplified briefing schedule would apply only if the appellant makes a written election.

For franchise and income tax appeals, the amount at issue includes all amounts in dispute, whether denominated as tax, interest, or penalty, for all taxable years covered by the appeal. If two or more appellants file a joint appeal, the amount at issue is determined separately for each appellant. The elective, simplified briefing schedule does not apply to innocent spouse appeals, appeals from a jeopardy determination, or appeals involving the corporate franchise and income taxes, other than the minimum franchise tax. Any dispute regarding its application will be resolved by the Chief Counsel.

Upon receipt of an appeal from an action of the FTB, the Board Proceedings Division will review the appeal to determine whether it is eligible for the elective, simplified briefing schedule. The Chief of Board Proceedings may contact the appellant to obtain more information and consult with

the Chief Counsel, if necessary. If an appeal is eligible, the Board Proceedings Division will send a notice advising the appellant that the appellant has 30 days to elect the simplified briefing schedule, that appellants who make such an election are eligible for pro bono representation through any program approved by the Board, that by making the election the appellant agrees to submit its appeal to the Board on the briefs without an oral hearing, and that the election becomes irrevocable once the FTB files its opening brief. The Chief Counsel will have discretion to revoke an election that was made by mistake in case appellants are still confused about their rights after reading the Board Proceedings Division's notice.

Appellants who make the election to apply the simplified briefing schedule will have their appeals decided with the same diligence and objectivity as any other appeal. However, the appeals process will be shortened. The perfected appeal will constitute the appellant's opening brief, the FTB will have 60 days from date the Board Proceedings Division acknowledges the appellant's election to file its opening brief, and the appellant may file a reply brief within 30 days of the date the FTB's opening brief is acknowledged. Thereafter, the Appeals Division will prepare a summary decision, which will be submitted to the Board as a non-appearance matter.

The elective, simplified briefing schedule is designed to shorten the appeals process for as many appellants as possible without compromising the quality of the Board's overall appellate review. By shortening the process for some appellants, staff hopes to conserve the Board's administrative resources so that they can be used to provide the new discretionary pre-hearing conferences (which are discussed below). Staff also hopes that the elective, simplified briefing schedule will provide a less intimidating avenue for unrepresented taxpayers, and an expedited procedure that will minimize the accrual of interest on outstanding liabilities.

Briefing Schedule for Innocent Spouse Appeals

Chapter 4 proposes a more detailed briefing schedule for innocent spouse appeals. Although the proposed briefing schedule is more complex than currently provided in the *Rules of Practice*, staff determined that the proposed schedule is necessary to account for the complexities resulting from multiple appellants with adverse interests. In addition, staff believes the proposed schedule is necessary to comply with recent statutory amendments requiring meaningful participation in the appeal for both spouses. (See Rev. & Tax. Code, § 18533, subd. (e)(3)(B) effective Jan. 1, 2004.)

The framework of the innocent spouse briefing schedule only differs from the general (default) briefing schedule because it gives the non-appealing spouse² the right to file an opening and reply brief, and allows the other parties to respond to those briefs. In addition, the innocent spouse briefing schedule contains a provision for conformity with federal determinations that become final

² The proposed regulation defines the "appealing spouse" as the spouse who files an appeal from the FTB's grant or denial of innocent spouse relief. The "non-appealing spouse" is the person with whom the appealing spouse filed a joint return, and in general agrees with the FTB's determination.

after the appeal is filed, in compliance with recent statutory amendments. (See Rev. & Tax. Code, § 18533, subd. (i), effective Jan. 1, 2004.)

Amicus (Non-Party) Briefs

The current *Rules of Practice* contain a general provision allowing the filing of amicus briefs; Chapter 4 continues to allow the filing of amicus briefs. Chapter 4, however, contains more detail and clarity regarding when and how such briefs may be filed and gives the Appeals Division authority to request amicus briefs. Also, no individual or entity may file more than one amicus brief, and the brief must be filed before the applicable briefing schedule is concluded.³ Chapter 4 retains the right of both parties to file responses to any amicus briefs. Staff believes that Chapter 4 provides much-needed clarity and consistency in the filing and processing of amicus briefs.

Discretionary Supplemental Briefing

The Board's current procedures recognize that the standard briefing schedule may not always result in the submission of adequate briefing and/or evidence. Likewise, Chapter 4 recognizes that its three briefing schedules may not always be sufficient and allows for supplemental briefing. Chapter 4 allows the Appeals Division, a Board Member, or the Board to request supplemental briefing from either or both parties. Supplemental briefing may be requested regardless of the briefing schedule utilized. The Appeals Division or a Board Member could request supplemental briefing prior to any scheduled oral hearing, whereas the Board could make a request at the oral hearing

In a minor departure from current procedures, Chapter 4 requires that the Board Chair be notified whenever a Board Member or the Appeals Division requests supplemental briefing prior to an oral hearing. This change is intended to allow the Board Chair to modify the hearing calendar, if necessary, to allow the supplemental briefing to proceed.

D. Chapter 4's Provisions for Requesting and Granting Oral Hearings

Chapter 4 continues the Board's current practice of allowing appellants to request oral hearings on appeals from actions of the FTB, with three modifications.

First, Chapter 4 requires appellants to file their requests for an oral hearing within 30 days after the conclusion of the briefing schedule; a late-filed request may still be accepted if the Chief Counsel

³ For example, if the general (default) briefing schedule is applicable and both the taxpayer and FTB take advantage of all briefing opportunities, then all amicus briefs must be filed before the taxpayer files its supplemental brief (i.e., the taxpayer's third and final brief). If the FTB chooses not to file a reply brief, then all amicus briefs must be filed before the taxpayer files its reply brief (i.e., the taxpayer's second brief). The requirement that all amicus briefs be filed before the conclusion of the briefing schedule is consistent with current procedure. The rationale for this requirement is that a non-party should not be able to delay the appeal or "whipsaw" either of the parties by filing an amicus brief late in the process.

finds reasonable cause. This change is intended to conserve staff resources by requiring appellants to decide whether they want an oral hearing before the Appeals Division prepares the appeal for submission to the Board.

Second, Chapter 4 permits the Board to hold separate hearings for the appealing and non-appealing spouses in an innocent spouse case. In order for separate oral hearings to be held, there must be a court order prohibiting the spouses from appearing together, or a determination by the Board Chair that having the spouses appear together would result in an unsafe, disruptive, or unjust hearing.

Third, Chapter 4 proposes a procedure for denying an oral hearing in two types of “res judicata” cases:⁴

- When the appeal involves a claim for refund stemming from the same assessment that was at issue in a prior appeal; and
- When the appeal involves an interest-abatement request that is simply a repeat of a prior request for abatement of the same interest.

A request for an oral hearing would be denied only if the Chief of Board Proceedings, the Chief Counsel, and the Board Chair agree that res judicata applies. Staff believes this change will conserve staff resources and save Board meeting time, and it is consistent with the res judicata provisions of the Revenue and Taxation Code. (See Rev. & Tax. Code, § 19802.)

E. Chapter 4’s Discretionary Pre-Hearing Conference Procedures

Currently, the Board’s *Rules of Practice* do not provide for the holding of any appeals conferences in appeals from the FTB. During the interested parties process, staff considered numerous comments and suggestions as to the feasibility and merits of holding appeals conferences (similar to those held in business taxes appeals). Ultimately, staff determined that mandatory appeals conferences were not feasible in all appeals from the FTB. However, staff believes that many of the benefits of appeals conferences can still be achieved by providing discretionary pre-hearing conferences for some cases set for oral hearing.

Staff determined that mandatory appeals conferences in appeals from the FTB are not feasible because:

- The Board Proceedings Division and the Appeals Division process over 1,000 appeals from the FTB each year, using only 15 staff positions (including eight attorneys). Adding mandatory appeals conferences to the FTB appeals process would represent an increased workload that existing staff resources could not absorb;

⁴ “Res judicata” is a judicial doctrine holding that, once a matter has been decided, that same matter should not be re-litigated and decided again. Revenue and Taxation Code section 19802 incorporates the doctrine of res judicata into California’s income tax administration laws. Under Chapter 4, res judicata would apply only when the same fact(s), law(s), and year(s) are at issue.

- The FTB's existing resources could not absorb the additional workload. In addition, appeals conferences might be duplicative of the statutory protest hearing process provided by FTB; and,
- Private practitioners expressed concern about the resources they and their clients would need to expend to comply with the additional procedural step of an appeals conference.

Thus, there appeared to be consensus among interested parties that mandatory appeals conferences were not well-suited to the FTB appeals process.

Instead of adding appeals conferences similar to those held in business taxes appeals, Chapter 4 provides for discretionary pre-hearing conferences in cases set for oral hearing. Under this process:

- The Appeals Division in its discretion may require that the parties attend a pre-hearing conference when the record does not adequately address all of the relevant factual and legal issues;
- Either party or a Board Member may request a pre-hearing conference;
- The Chief Counsel in his or her discretion may deny a party's request if he or she determines that a pre-hearing conference would be unproductive and a misuse of resources;
- The Appeals Division will be able to more fully develop appeals, when necessary, and thereby help the Board make better use of its hearing time, without expending BOE, FTB, and taxpayer resources unnecessarily.

Staff believes that discretionary pre-hearing conferences in cases set for oral hearing will be a welcome and productive addition to the FTB appeals process, without creating an overbearing workload or unnecessarily lengthening the appeals process.

F. Chapter 4's Procedures for Issuing All Three Types of Board Decisions and Adopting Formal Opinions (Including Dissenting and Concurring Opinions)

Currently, the Board issues three types of written decisions on appeals from the FTB:

- Summary Decisions are staff-prepared decisions containing findings of fact and conclusions of law. A Summary Decision is generally prepared when the appellant does not request an oral hearing; it is submitted to the Board for adoption as a non-appearance matter;
- Letter Decisions are brief explanations of the Board's decision, usually prepared at the conclusion of an oral hearing;
- Formal Opinions create precedent binding upon the Board and the FTB. A Formal Opinion is sometimes prepared at the Board's request, and sometimes upon staff recommendation. A Formal Opinion must be adopted by the Board.

Chapter 4 maintains and clarifies current procedures by describing the type of decisions, explaining their meaning, and identifying Formal Opinions as being citable as precedent.

The Board currently has no formal criteria for the adoption of Formal Opinions. Chapter 4 proposes to adopt criteria from the California Rules of Court that govern the publication of appellate opinions. Those criteria include: whether the decision would establish a new rule of law, apply an existing rule to new facts, or modify or repeal an existing rule; whether the decision would create or resolve a conflict in law; whether the decision involves an issue of continuing public interest; and whether the decision makes a contribution to the law by reviewing the development of a legal rule. Staff believes that these widely-accepted criteria will create a rational and consistent foundation for the adoption of Formal Opinions.

The current *Rules of Practice* do not preclude the Board's issuance of dissenting and/or concurring opinions. The Board, however, currently has no formal procedure for the preparation of dissenting or concurring opinions. Chapter 4 proposes to add new procedures for the preparation of dissents (when a Member disagrees with the result of a Formal Opinion) and concurrences (when a Member agrees with the result but not the rationale of a Formal Opinion). The proposed procedures would permit a dissenting or concurring Board Member to order the Appeals Division to prepare an opinion reflecting that Member's views. The dissenting or concurring Board Member would give the order at a Board Meeting, no later than the Board Meeting at which the underlying Formal Opinion is adopted. Upon receiving such an order, the Appeals Division would prepare the dissent or concurrence. The dissent or concurrence would then be approved at a Board Meeting by the Member who ordered its preparation. Staff hopes that these procedures will provide Board Members with a clear and consistent avenue to express their views on controversial Formal Opinions.

G. Chapter 4's Procedures for Imposing Frivolous Appeal Penalties

Pursuant to Revenue and Taxation Code section 19714, the Board has the authority to impose penalties on taxpayers who file frivolous appeals. The Board does not currently have any formal criteria for whether to impose such a penalty, or in what amount. Chapter 4 proposes several criteria gleaned from staff's experience and the comments of interested parties. Those criteria include: whether the taxpayer is making arguments that the Board and courts have repeatedly rejected; whether the taxpayer is making the same arguments that he or she made in prior appeals; whether the taxpayer filed the appeal with the intent of delaying the legitimate collection of tax owed; and whether the taxpayer has a history of filing frivolous appeals or failing to comply with California's tax laws. Staff believes these criteria will provide a rational and consistent foundation for the imposition of frivolous appeal penalties in appropriate cases, as well as provide much-needed notice to taxpayers.

H. Chapter 4's Clarification of the Request for Rehearing and Rehearing Processes

The current *Rules of Practice* contain very little detail regarding petitions for rehearing, granting or denying those petitions, and holding rehearings when the petitions are granted. In order to provide clarity and notice to taxpayers and the FTB, Chapter 4 proposes a step-by-step process beginning with the issuance of a decision and ending with the holding of a rehearing on the appeal. The proposed process includes briefing schedules, deadlines, and criteria for granting or denying rehearings.

Chapter 4's proposed procedures begin with the issuance of the Board's decision on an appeal. A party who disagrees with that decision has 30 days from the date of the decision to file a Petition for Rehearing. That 30-day period is fixed by statute and, therefore, cannot be extended even for reasonable cause or for the Board's failure to mail a notice. The proposed regulations set forth the kinds of information that must be present in a Petition for Rehearing, and grant the parties 30 days to perfect the Petition for Rehearing if some information is missing. Thirty days after the filing of a perfected Petition for Rehearing, the non-filing party will be allowed to file a responsive brief. Once the briefs are filed, the Appeals Division will prepare a Decision on Petition for Rehearing, which will recommend that the Board either grant or deny the rehearing. The Decision on Petition for Rehearing will be presented to the Board for adoption as a non-appearance matter. The decision is not citeable unless the Board votes to adopt it as a Formal Opinion. With regard to adopting criteria for granting or denying a rehearing, Chapter 4 proposes to use the same criteria that the Board adopted in the *Appeal of Wilson Development* (94-SBE-007), decided on October 5, 1994.

If the Board grants a rehearing, Chapter 4 allows the filing party (i.e., the party who requested the rehearing) 30 days from the date of the Board's decision to file an opening brief. The non-filing party then has 30 days from the date of the acknowledgment of the opening brief to file a reply brief. The filing party has 30 days thereafter to file its own final reply brief. At the conclusion of briefing, the provisions applicable to hearings and decisions govern the subsequent rehearing and Board decision.

Staff believes that Chapter 4's proposed procedures utilize and improve the best parts of the Board's current informal process for handling petitions for rehearing. Staff is confident that the proposed procedures will help taxpayers and the FTB understand what their rights and obligations are when a Petition for Rehearing is filed. Staff is also confident that the proposed procedures provide a fair, efficient, and consistent basis for processing Petitions for Rehearing.

III. Current Status

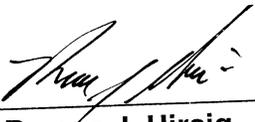
Chapter 4, *Appeals from Actions of the Franchise Tax Board*, is presented for the Board's approval in concept. Staff will present its proposed language for Chapter 4 to the Board for its approval after receiving direction from the Board on the concepts. Once the Board has approved the proposed language for all five chapters of the New Rules, staff will ask the Board for approval to publish the initial notice of rulemaking.

IV. Recommendation

Staff recommends the Board grant concept approval of Chapter 4, *Appeals from Actions of the Franchise Tax Board*.

KC:jlh
Chief Counsel/Chap.4

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Mr. David Gau, MIC: 63
Ms. Anita Gore, MIC: 86
Ms. Randie L. Henry, MIC: 43
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Approved 
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