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12 **BOARD OF EQUALIZATION**
13 **STATE OF CALIFORNIA**

14 In the Matter of the Appeal of:) **HEARING SUMMARY**
15) **PERSONAL INCOME TAX APPEAL**
16) Case No. 487053
17 **HARVINDER SINGH PAHAL AND**)
18 **SATVINDER KAUR**¹)

<u>Year</u>	<u>Proposed Assessment</u> ²
2004	\$4,120

19 Representing the Parties:

20 For Appellants: Matthew J. Staub, Tax Appeals Assistance Program³

21 For Franchise Tax Board: Jean Cramer, Tax Counsel IV

22
23 **QUESTIONS:** (1) Whether the Board has jurisdiction to determine that appellants' tax liability for
24 2004 has been discharged in bankruptcy.

25
26 ¹ Appellants reside in Sacramento, California.

27 ² Respondent should be prepared to provide the accrued interest amount at the time of the oral hearing.

28 ³ Appellants filed their appeal letter; Matthew J. Staub, a law student who is participating in the Tax Appeals Assistance Program (TAAP), submitted appellants' reply brief and supplemental brief.

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1 (2) Whether respondent should be estopped from assessing the proposed tax and/or
2 related interest pursuant to the doctrine of equitable estoppel.

3 (3) Whether, in the alternative, appellants have shown that respondent's proposed
4 assessment is erroneous.

5 HEARING SUMMARY

6 Background

7 Appellants timely filed their 2004 tax return. Based on an audit determination of
8 unreported income, respondent issued a Notice of Proposed Assessment (NPA) to appellants on
9 October 26, 2007. The audit determination of unreported income totaled \$77,294, which resulted in
10 additional tax of \$4,120, plus applicable interest. (Resp. Op. Br., exhibit A.) On December 15, 2007,
11 appellants timely protested the NPA. Appellants argued that the amount determined by the audit as
12 unreported income was actually informal loans or gambling losses.

13 Subsequently, appellants filed for a Chapter 7 bankruptcy on September 3, 2008. On
14 December 15, 2008, appellants were issued a Discharge of Debtor Order by the United States
15 Bankruptcy Court for the Eastern District of California. (Resp. Op. Br., exhibit B.) Respondent was
16 included on the list of creditors for appellants' bankruptcy proceeding. (App. Reply Br., exhibit A.)

17 On March 30, 2009, respondent issued a Notice of Action (NOA) to appellant that
18 affirmed the NPA of additional tax of \$4,120.00 for the 2004 tax year and interest through the date of
19 the NOA of \$823.07. On April 22, 2009, appellants filed this timely appeal.

20 Contentions

21 Appellant's Contentions

22 Appellants assert that their proposed assessment for 2004 was discharged in bankruptcy.
23 (Appeal Letter.)

24 Appellants contend that the proposed tax liability would have become final if they had
25 not protested the NPA. In that event, appellants contend, the assessment would have been final and,
26 thus, dischargeable in bankruptcy. Appellants argue that it is "fundamentally unfair" to require them to
27 pay the tax when another taxpayer in the same situation who may have ignored the NPA and failed to
28 protest would not have to pay the same tax. Appellants also contend that the tax was "assessed" and,

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1 therefore, dischargeable in bankruptcy, as a result of their protest of the NPA. Appellants state that they
2 “protested the substance of their 2004 tax liability and not the accuracy of the calculation of the
3 liability.” On that basis, appellants contend that the “calculation was complete upon the protest of the
4 NPA” and the NOA “represented the formal act of fixing the tax liability.” Appellants conclude that
5 under the reasoning of *In re King* (9th Cir. 1992) 961 F.2d 1423, “appellants’ tax was assessed” and
6 should have been discharged in bankruptcy. (App. Reply Br., p.2.)

7 Appellants agree that the Board does not have jurisdiction to decide whether a tax
8 liability has been discharged in bankruptcy. However, appellants contend that the Board should use its
9 equitable power to adopt their position in an effort to preserve the time and resources of the Bankruptcy
10 Court. (App, Reply Br., p.2.) Appellants argue that they should prevail on the grounds of equitable
11 estoppel. (App. Supp. Br., pp. 1-2.) Specifically, appellants argue that the four elements of equitable
12 estoppel are met here:

- 13 1) FTB had complete knowledge of appellants’ bankruptcy proceedings and thus was
14 apprised of the facts. Nonetheless, respondent issued and NOA after the resolution of
15 the proceedings.
- 16 2) Respondent intended appellants to act upon its conduct in that respondent induced
17 appellants to appeal the NOA. However, the NOA did not mention the bankruptcy
18 proceedings or the fact that failure to appeal would result in the assessment becoming
19 final and, therefore, dischargeable in bankruptcy.
- 20 3) Appellants were ignorant of the true facts in that they were not aware that their appeal
21 would not allow the assessment to become final. Nor were appellants aware that this
22 Board does not have jurisdiction over bankruptcy matters.
- 23 4) Appellants relied on respondent’s conduct to their detriment.

24 Alternatively, appellants argue that their deposits in their checking and savings accounts were actually
25 borrowed monies to support their family during difficult financial times. Since these deposits were not
26 income, but were borrowed monies, appellants assert that they should not have been determined to have
27 a tax liability. (App. Reply Br., p.2.)

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1 Respondent's Contentions

2 Respondent argues that the Board does not have jurisdiction to consider whether the
3 proposed assessment for appellants' 2004 tax year was discharged in bankruptcy. Nonetheless,
4 respondent contends that the proposed assessment at issue in this appeal was not discharged in
5 bankruptcy. Respondent argues that a tax liability cannot be discharged until the assessment became
6 final, whereas here the 2004 proposed assessment is still not final.

7 With respect to appellants' argument, that if they failed to protest their tax liability it
8 would have become final and thus discharged in bankruptcy, respondent argues that the issue is moot
9 because appellants did in fact protest the NPA. Respondent contends that assessment occurs for
10 bankruptcy dischargeability purposes when the assessment is final. As a matter before this Board,
11 respondent asserts, the assessment is not final and, thus, is not dischargeable. In addition, respondent
12 notes that during protest the tax liability was not collectible (the tax agencies' opportunity to collect the
13 tax being the purpose for the waiting periods prior to which a bankruptcy petition may be filed in order
14 to discharge a tax liability). Respondent contends that this was considered a material factor by the Court
15 of Appeal in *In Re King supra*, as to when the assessment occurs for bankruptcy purposes. (Resp. Reply
16 Br., p.2.)

17 Respondent thus maintains that the assessment in this appeal has not become final,
18 because the Board has not issued its decision, and therefore the tax liability could not have been
19 discharged in bankruptcy. Therefore, respondent asserts that it can properly assess of \$4,120, plus
20 applicable interest, against appellants for the 2004 tax year (assuming the Board sustains its action
21 issuing the NOA). (Resp. Opening Br., p.2.)

22 Applicable Law

23 Discharge in Bankruptcy

24 The Bankruptcy Code enumerates certain classes of debts which are not dischargeable.
25 (11 U.S.C. § 523(a)(1)-(12).) Bankruptcy Code sections 523(a)(1) and 507(a)(8) provide that taxes are
26 not dischargeable if, at that time the bankruptcy is filed, the taxes are "assessable," but not finally
27 assessed. Decisions as to whether a particular debt has been discharged by the bankruptcy court are
28 within the exclusive jurisdiction of the bankruptcy court as to debts within classes provided for under

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1 sections 523(a)(2), (a)(4), and (a)(6). The federal and state courts have concurrent jurisdiction to pass
2 on dischargeability of debts in the remaining classes, which includes tax debts. (*In re Aldrich* (9th Cir.
3 BAP, 1983) 34 B.R. 776.) The concurrent jurisdiction of the state courts relates only to those courts of
4 general jurisdiction. However, this Board's jurisdiction is of a limited nature and bankruptcy discharge
5 issues are specifically proscribed. (Cal. Code Regs., tit. 18 § 5412, subd. (b)(3).)

6 In addition, this Board previously held that it lacks jurisdiction to determine whether a
7 discharge in bankruptcy applies to respondent's assessment of tax, penalties, and interest. (*Appeal of*
8 *Robert G. and Jean C. Smith*, 81-SBE-145, Oct. 27, 1981; *Appeals of Fred R. Dauberger, et al.*, 82-
9 SBE-082, Mar. 31, 1982.) The determination of dischargeability must therefore be raised in a different
10 forum, such as a bankruptcy court.

11 Equitable Estoppel

12 Equitable estoppel is applied against the government only in rare and unusual
13 circumstances, when all of its elements are present, and its application is necessary to prevent manifest
14 injustice. (*California Cigarette Concessions, Inc. v. City of Los Angeles* (1960) 53 Cal.2d 865, See
15 *Appeal of Richard R. and Diane K. Smith*, 91-SBE-005, Oct. 9, 1991.) The taxpayer, as the party
16 claiming the application of estoppel, has the burden of proving that all of the elements are present.
17 (*Appeal of Western Colorprint*, 78-SBE-071, Aug. 15, 1978; *Appeal of U.S. Blockboard Corporation*,
18 67-SBE-038, July 7, 1967.) The four elements of equitable estoppel are: (1) the government agency
19 must be shown to have been aware of the actual facts; (2) the government agency must be shown to have
20 made an incorrect or inaccurate representation to the relying party and intended that its incorrect or
21 inaccurate representation would be acted upon by the relying party or have acted in such a way that the
22 relying party had a right to believe that the representation was so intended; (3) the relying party must be
23 shown to have been ignorant of the actual facts; and (4) the relying party must be shown to have
24 detrimentally relied upon the representations or conduct of the government agency. (*Strong v. County of*
25 *Santa Cruz* (1975) 15 Cal.3d 720; *Appeal of Western Colorprint, supra*; *Appeal of Priscilla L.*
26 *Campbell*, 79-SBE-035, Feb. 8, 1979.) Detrimental reliance is present only if respondent's actions
27 cause the taxpayer to take action which leads to increased tax liability. (*Appeal of Robert C. and Betty L.*
28 *Lopert*, 82-SBE-011, Jan. 5, 1982.) Where one of these elements is missing, there can be no estoppel.

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1 (*Hersch v. Citizens Savings & Loan Assn.* (1983) 146 Cal.App.3d 1002, 1011.)

2 The FTB is an administrative agency, and it does not have the legal authority to interpret
3 a statute in such a way as to change its meaning or effect. (*Appeal of Melvin D. Collamore*, 72-SBE-
4 031, Oct. 24, 1972.) Thus, when the FTB's instructions or online programs are alleged to be misleading,
5 taxpayers must follow the law, rather than the instructions. (*Ibid.*) Further, the general rule with respect
6 to applying equitable estoppel in tax matters is that the state cannot be estopped because of acts of its
7 employees (in providing erroneous administrative tax rulings) from collecting the tax due from the
8 taxpayer. (See *Market S.R. Co. v. Cal. Bd. of Equalization* (1955) 137 Cal.App.2d 87, 103; *La Societe*
9 *Francaise de Bienfaisance Mutuelle v. Cal. Employment Com.* (1943) 56 Cal.App.2d 534, 555.)

10 Accuracy of Assessments

11 Respondent's proposed assessment is presumed correct, and the taxpayer bears the
12 burden of proving error. (*Appeal of Sheldon I. and Helen E. Brockett*, 86-SBE-109, June 18, 1986.)
13 Unsupported assertions will not satisfy appellants' burden of proof. (*Appeal of Aaron and Eloise*
14 *Magidow*, 82-SBE-274, Nov. 17, 1982.) In the absence of uncontradicted, credible, competent, and
15 relevant evidence showing error in respondent's determinations, they must be upheld. (*Appeal of Oscar*
16 *D. and Agatha E. Seltzer*, 80-SBE-154, Nov. 18, 1980.)

17 STAFF COMMENTS

18 Discharge in Bankruptcy

19 With respect to appellants' bankruptcy contentions, by regulation and precedent, the
20 Board does not have jurisdiction to determine whether a discharge in bankruptcy applies to respondent's
21 assessment of tax, penalties, and interest. (*Appeal of Robert G. and Jean C. Smith, supra*; *Appeals of*
22 *Fred R. Dauberger, et al., supra*.) Appellants must raise this argument in the appropriate court.

23 Although appellants argue that the Board should use its "equitable power" to preserve the
24 time and resources of the Bankruptcy Court, there has been no authority cited for such "equitable
25 power" to determine appellants' bankruptcy contentions. Moreover, it appears to the Appeals staff that
26 appellants' tax liability would not have been discharged in bankruptcy because Bankruptcy Code section
27 523(a)(1)(A) specifically excludes from discharge all taxes that are entitled to priority under Bankruptcy
28 Code section 507(a). Thus, appellants' discharge in bankruptcy does not necessarily mean they are

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1 freed from all of their obligations. Section 507(a) provides a priority for “unsecured claims of
2 governmental units to the extent that such claims are for a tax ... not assessed before, but assessable,
3 under applicable law or by agreement, after the commencement of the case.” (11 U.S.C. §
4 507(a)(8)(A)(iii).) Therefore, a tax assessment needs to be assessed prior to appellants’ filing of their
5 petition in bankruptcy in order for it to be discharged.

6 Here, appellants’ tax assessment was not assessed prior to their filing of their petition in
7 bankruptcy in 2008. An NPA does not constitute an assessment until it becomes final. An NPA
8 becomes final after 60 days if it is not protested. (Rev. & Tax. Code, § 19042.) Appellants’ protested
9 the NPA on December 15, 2007, therefore the NPA did not become final. If an NPA is protested and an
10 NOA is issued, then the assessment becomes final after 30 days if the NOA is not appealed. (Rev. &
11 Tax. Code, §§ 19045 and 19048.) Appellants’ filed a timely appeal to this Board on April 22, 2009.
12 Therefore, the assessment will not become final until 30 days after this Board’s decision on this appeal.
13 (Rev. & Tax. Code, § 19048.) As a result, it appears that respondent’s tax assessment was not final
14 before appellants’ bankruptcy petition was filed, and thus it would have been exempt from discharge
15 under Bankruptcy Code section 523(a)(1)(A).

16 Equitable Estoppel

17 Since appellants have the burden of proving that all the elements of equitable estoppel are
18 present, they should be prepared at the hearing to show that all four elements have been met. Appellants
19 especially should focus on establishing the second element, i.e. that respondent made an inaccurate or
20 incorrect representation, and intended appellants to rely on that representation, given that respondent
21 simply issued an NOA pursuant to R&TC section 19033, with the information required pursuant to
22 R&TC section 19034; and further, according to appellants characterization, it was appellants’ own
23 misunderstanding of the bankruptcy law that caused them to appeal the NOA.

24 Appellants should also focus on establishing the fourth element, “detrimental reliance”,
25 because it appears that respondent made no representation that appellants could rely on, and detrimental
26 reliance is only present if respondent’s actions cause the taxpayers to take actions which lead to an
27 increased tax liability. (*Appeal of Robert C. and Betty L. Lopert, supra.*) Appellants argue that they
28 were misled to their detriment since respondent issued the NOA over three months after the bankruptcy

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1 proceedings, and appellants thought the only way to dismiss their tax debt would be to appeal the NOA.
2 To date, appellants have not provided any evidence that respondent made any representations about the
3 necessity of appealing the NOA. Also, since the NPA was issued before appellants filed their petition in
4 bankruptcy, and the NOA merely affirmed the NPA, respondent's action issuing the NOA did not
5 increase appellants' tax liability. Staff notes that the state generally cannot be estopped because of acts
6 of its employees from collecting the tax due from the taxpayer; accordingly, should equitable estoppel
7 be found to apply here, it would not be applicable to the tax the Board determines is due.

8 Accuracy of the Assessment

9 Finally, respondent's proposed assessment is presumed correct and taxpayers bear the
10 burden of proving error. Thus, appellants should be prepared to prove that the FTB audit, which
11 resulted in the NPA, is erroneous. Specifically, appellants should be prepared to show by
12 uncontradicted, credible, competent, and relevant evidence that they did not have a tax liability by, for
13 example, showing the deposits in their checking and savings accounts were borrowed monies to support
14 their family during difficult financial times, and not income.

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