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BOARD OF EQUALIZATION
STATE OF CALIFORNIA

In the Matter of the Appeal of:) **HEARING SUMMARY**
) **PERSONAL INCOME TAX APPEAL**
)
VICTORIA SOUFFLET¹) Case No. 461166
)
)

	<u>Year</u>	<u>Claim For Refund</u>
	2001	\$622 ²

Representing the Parties:

For Appellant: L. Tracy Mackenzie, TAAP³
For Franchise Tax Board: Delinda R. Tamagni, Tax Counsel

¹ Appellant resides in Siskiyou County, California.

² This is the amount at issue based on the appeal letter. In its opening brief, however, respondent states that appellant's 2001 account displays a barred overpayment credit of \$700 due to interest. (Resp. Opening Br., fn. 1, exhibit A.) As discussed below, respondent has now conceded that appellant is entitled to a refund of her 2001 income tax withholding credit of \$497 because it constitutes non-amnesty payments. (Resp. Reply Br., p. 2.) In addition, as discussed below, in May 2008 respondent refunded \$41.61 to appellant. The current amount at issue thus appears to be \$161.39 (\$700.00 - \$497.00 - \$41.61).

³ Appellant submitted the appeal letter and the Supplemental Information letter. Kalina Laleva, a member of the Tax Appeals Assistance Program (TAAP), submitted appellant's reply brief. Tina Kaur, another member of TAAP, submitted appellant's supplemental brief. At the time of the hearing, L. Tracy Mackenzie, another member of TAAP, represents appellant.

1 QUESTION: Whether the Board has jurisdiction to consider a claim for refund of payments
2 appellant made through the tax amnesty program.

3 HEARING SUMMARY

4 Background

5 Appellant timely filed a 2001 California Resident Income Tax Return (Form 540). On
6 her return, appellant reported \$1,155 of wages, federal adjusted gross income of \$31,927, California
7 adjustments (subtractions) of \$4,401, itemized deductions of \$6,432, taxable income of \$21,094, and a
8 total tax of \$514. Appellant claimed an exemption credit of \$79 and reported \$622 of other taxes on
9 an early taxable distribution from a qualified retirement plan from Form 3805P (Additional Taxes on
10 Qualified Plan (Including IRAs) and other Tax-Favored Account). On her schedule CA (540),
11 appellant reported total taxable pensions and annuities distribution of \$24,871.⁴ After applying \$497
12 of California income tax withheld, appellant reported tax due in the amount of \$560. (App. Opening
13 Br., Attachment.)

14 Appellant did not remit payment of the balance shown as due on the 2001 return.
15 Respondent consequently issued a Return Information Notice (RIN) dated May 3, 2002, which
16 imposed an underpayment penalty of \$28, plus applicable interest. (Resp. Opening Br., exhibit B.).
17 On November 26, 2002, respondent also imposed a collection cost recovery fee of \$101. (*Ibid.*)

18 On or about January 10, 2005, respondent sent an amnesty notice to appellant. (Resp.
19 Opening Br., p. 2, exhibit C.) Appellant submitted to respondent a completed Income Tax Amnesty
20 Application, which she apparently signed on March 8, 2005. (*Id.*, exhibit D.) Pursuant to the tax
21 amnesty program, respondent and appellant executed an amnesty installment agreement and
22 respondent abated the underpayment penalty and collection cost fee for tax year 2001. (*Id.*, exhibit A.)
23 From June 10, 2005, to May 30, 2006, appellant made installment payments totaling \$694.17, which
24 satisfied her tax and interest liability for tax year 2001. (*Ibid.*)

25
26
27 ⁴ Staff notes that the file does not contain a copy of any 2001 Form 1099-R, Distributions From Pensions, Annuities,
28 Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc. with respect to appellant's early distribution of a qualified
retirement plan of \$24,871. Staff further notes that attached to the appeal letter is a print out from appellant's tax preparer
that lists the following Form 1099-R information: the payer, "College Ret. Eq. Fund," distributed to appellant a gross and
taxable amount of \$24,871 (distribution code 1) and *federal and state taxes were withheld in the amount of \$4,974 and \$497,*
respectively. Staff notes that distribution code 1 generally indicates no known exception to the early distribution penalty.

1 On May 15, 2007,⁵ appellants filed an amended 2001 return (FTB Form 540X) on
2 which she claimed a refund of \$622, because she was completely and totally disabled at the time of the
3 early distribution and therefore exempted from the early distribution tax. (App. Opening Br.,
4 Attachment.) In a cover letter dated May 10, 2007, which she submitted with her amended 2001
5 return, appellant stated that in April 2007 she received a refund in the amount of \$7,316.93 from the
6 Internal Revenue Service (IRS) for the 2001 tax year and she believed she was also entitled to a refund
7 from respondent. (*Id.*)

8 In a letter dated May 6, 2008, respondent informed appellant that it cancelled the
9 penalty for an early distribution of a qualified retirement plan and partially allowed her claim for
10 refund for tax year 2001. (App. Opening Br., Attachment.) Respondent further stated in this letter
11 that it would only refund her payment of \$36.17, which it received on May 30, 2006, because it was an
12 overpayment made within one year of the filing of the claim for refund on May 15, 2007. (*Ibid.*)
13 According to respondent, it subsequently refunded \$41.61 (\$36.17 plus \$5.44 of interest) to appellant
14 and denied the remainder of the overpayment due to the running of the four-year and one-year statutes
15 of limitations. (Resp. Opening Br., p. 2.)

16 This timely appeal followed.

17 Appellant's Contentions

18 On appeal, appellant does not dispute that she signed an amnesty application and made
19 payments from June 10, 2005, to May 30, 2006 in satisfaction of her 2001 tax liability pursuant to an
20 amnesty installment plan. Appellant contends that she is entitled to a full refund of the \$622 she paid
21 as a penalty for an early distribution from a qualified retirement plan in 2001 because she was
22 completely and totally disabled at the time of the distribution. Citing Revenue & Taxation Code
23 (R&TC) section 19311, appellant contends that respondent should make a refund of the \$622 because
24 the IRS suspended the relevant statute of limitations due to appellant's physical disability and fully
25

26 ⁵ Staff notes that respondent's May 6, 2008, letter states that appellant filed her amended 2001 return on May 15, 2007,
27 whereas respondent's opening brief states that it was filed on June 15, 2007. Staff assumes that the amended return was in
28 fact filed on May 15, 2007 because respondent issued a refund of a May 30, 2006, payment of \$36.17 plus interest pursuant
to a one-year statute of limitations.

1 refunded the federal early distribution penalty appellant paid for tax year 2001.

2 Appellant contends that the tax amnesty program does not bar her claim for refund
3 because she did not actually owe any taxes in 2001 and thus did not receive amnesty on any penalties
4 or fees for 2001. Appellant contends she applied for amnesty and made payments in satisfaction of
5 her 2001 tax liability pursuant to an amnesty installment plan based on an erroneous belief that she
6 owed taxes in 2001. Appellant contends that the tax amnesty program's purpose is to recover
7 outstanding tax revenue and it is not intended to collect revenue from taxpayers who mistakenly paid
8 taxes due to their physical impairments. Appellant contends that it is against public policy to refuse
9 refunds or credits on taxes not owed and it sends the message that California taxpayers should not pay
10 their taxes. Appellant contends that the State of California was unjustly enriched because she
11 mistakenly made payments in good faith pursuant to the amnesty installment plan. Appellant contends
12 that R&TC section 19372, subdivision (e), violates her procedural due process rights under the United
13 States and California Constitutions and is therefore unenforceable in its entirety.⁶

14 Respondent's Contentions

15 Respondent concedes that under R&TC section 19316 the statute of limitations for
16 appellant's claim for refund, which is set forth in R&TC section 19306, is suspended from April 15,
17 2002, to the present due to appellant's financial disability. Respondent further concedes that appellant
18 has established that the IRS determined she was exempt from the federal penalty for early distribution
19 from a qualified retirement plan due to her total and permanent disability. Accordingly, respondent
20 concedes that appellant is also exempt from the California penalty for early distribution from a
21 qualified retirement plan in the amount of \$622, because the relevant California and federal law are the
22 same. For these reasons, respondent concedes that appellant is entitled to a refund of her income tax
23 withholding credit of \$497 because the withholding payments were not made under the amnesty
24 program.

25 With respect to the portion of appellant's claim for refund in excess of the \$497

27 ⁶ In light of respondent's concession that the relevant statute of limitations is suspended, staff does not discuss appellant's
28 contentions with respect to the statute of limitations.

1 withholding credit, respondent contends that appellant made these payments in satisfaction of her 2001
2 tax liability pursuant to the amnesty installment agreement. Respondent contends that appellant
3 waived her right to file a claim for refund or credit for tax year 2001 on the amounts for which she
4 applied for amnesty. Respondent asserts that the amnesty application appellant signed states in the last
5 paragraph that appellant is waiving her right to file a claim for refund or credit on the amounts subject
6 to amnesty. Respondent therefore contends that the Board does not have jurisdiction to consider
7 appellant's claim for refund of payments she made through the amnesty program. Respondent
8 contends that it erroneously refunded \$41.61 to appellant pursuant to its May 6, 2008, letter.
9 Respondent also contends that the Board does not have jurisdiction to consider constitutional issues
10 appellant raised in her appeal.

11 Applicable Law

12 2.5 Percent Tax on Early Distribution

13 Internal Revenue Code (IRC) section 72 governs distributions from qualified retirement
14 plans. IRC section 72 imposes an additional tax of 10 percent of the amount of the distribution unless
15 the distribution falls within an exception. There is an exception to the tax penalty for early
16 distributions from individual retirement plans attributable to the employee's being totally disabled.
17 (Int. Rev. Code, § 72, subd. (t)(2)(A)(iii).) R&TC section 17085 conforms to, but modifies, IRC
18 section 72. IRC section 72(t)(1) provides that, if a taxpayer receives an early distribution from a
19 qualified retirement plan, the taxpayer's tax shall be increased by an amount equal to 10 percent of the
20 portion of the amount that is includible in gross income. R&TC section 17085, subdivision (c)(1)
21 modifies the 10 percent to read 2.5 percent. There is an exception to the tax penalty for early
22 distributions from individual retirement plans attributable to the employee's being totally disabled.
23 (Int. Rev. Code, § 72, subd. (t)(2)(A)(iii).)

24 Statute of Limitations

25 The relevant statute of limitations is set forth in R&TC section 19306. R&TC section
26 19306 generally requires taxpayers to file a claim for refund within the later of: (1) four years from
27 the date the return was filed (if timely filed within the specified extension periods); (2) four years after
28 the due date of the return (without regard to any extensions of time to file); or (3) one year from the

1 date of the overpayment.

2 The statute of limitations may be extended in certain cases if there are federal
3 adjustments. Under R&TC section 19311, subdivision (a)(1), a refund claim “resulting from the
4 [federal] adjustments” may be filed within two years from the date of the final federal determination.
5 R&TC section 18622, subdivision (d), defines the date of the “final federal determination” as the date
6 on which the adjustment is assessed pursuant to IRC section 6203.

7 R&TC section 19316 tolls the statute of limitations during a period of “financial
8 disability,” which is defined by the statute as meaning that the taxpayer was unable to manage his or
9 her financial affairs due to a medically determinable physical or mental impairment that is either
10 deemed to be a terminal impairment or is expected to last for a continuous period of not less than 12
11 months. (Rev. & Tax. Code, § 19316, subs. (a) & (b)(1).) An individual taxpayer will not meet the
12 provisions of R&TC section 19316 if, for any period, the individual’s spouse, or any other person, is
13 legally authorized to act on the individual’s behalf in financial matters. (Rev. & Tax. Code, § 19316,
14 subd. (b)(2).) In order to demonstrate the existence of a financial disability, an appellant must submit
15 a signed affidavit from a physician that explains the nature and duration of any physical or mental
16 impairments. (*Appeal of James C. and Florence Meek*, 2006-SBE-001, Mar. 28, 2006.) In addition,
17 an appellant must show that he or she satisfies the strict definition of “financial disability” such that he
18 or she could not manage his or her financial affairs. (*Id.*) It is not sufficient to show that an appellant
19 could not engage in a regular occupation or that he or she was “disabled” under other statutory
20 definitions of disability. (*Id.*) In accordance with R&TC section 19316, respondent has published
21 Form 1564 to allow taxpayers to substantiate a financial disability. Here, the statute of limitations is
22 not at issue because respondent concedes that it is tolled from April 15, 2002, to the present because
23 appellant has shown she is financially disabled within the meaning of R&TC section 19316. (Resp.
24 Reply Br., pp. 1-2.)

25 Tax Amnesty Program

26 R&TC sections 19730 through 19738 set forth the tax amnesty program for taxpayers
27 subject to the Personal Income Tax Law and the Corporation Tax Law. The tax amnesty program was
28 conducted during the two-month period beginning February 1, 2005, and ending March 31, 2005, and

1 applied to tax liabilities for taxable years beginning before January 1, 2003. If an eligible taxpayer fully
2 paid the taxpayer's unpaid tax obligations and met all of the other requirements of the amnesty program,
3 respondent waived all unpaid penalties and fees imposed, and no criminal action would be brought
4 against the taxpayer for years subject to the amnesty program.

5 The amnesty program might be described as employing a "carrot and stick" approach.
6 On the one hand, the amnesty program provides an opportunity for a taxpayer to identify and pay unpaid
7 tax obligations and, in return, obtain a waiver of penalties and fees that might otherwise have been
8 imposed. On the other hand, if a taxpayer underpaid his or her taxes during a period prior to January 1,
9 2003, and failed to take advantage of the amnesty program, R&TC section 19777.5 imposes an amnesty
10 penalty. R&TC section 19777.5 generally provides that, for each tax year for which amnesty could have
11 been requested by the taxpayer, the amnesty penalty will be imposed in an amount equal to 50 percent of
12 interest accrued on unpaid tax as of the last day of the amnesty period (March 31, 2005). The amnesty
13 penalty is imposed in addition to any other applicable penalties.

14 R&TC section 19732, subdivision (e), severely limits the ability of taxpayers to file a
15 refund claim with respect to any amounts paid in connection with the tax amnesty program by providing
16 that "[n]otwithstanding Chapter 6 (commencing with Section 19301), a taxpayer may not file a claim for
17 refund or credit for any amounts paid in connection with the tax amnesty program under this chapter."
18 In accordance with R&TC section 19732, subdivision (e), the Income Tax Amnesty Application
19 provides, "I understand that by signing this application and completing amnesty, I give up my right to
20 protest, appeal, or file a claim for refund or credit on those amounts for which I have selected amnesty."
21 (Resp. Opening Br., exhibit D.)

22 Income Tax Withholding Credit

23 An income tax withholding credit is considered paid as of the due date of the return
24 (Rev. & Tax. Code, § 19002, subd. (c)). Here, appellant's income tax withholding credit of \$497
25 would be considered paid as of April 15, 2002.

26 STAFF COMMENTS

27 It appears that appellant would not be entitled to any refund or credit of any taxes,
28 penalties, fees or interest paid for tax year 2001 for payments made through the tax amnesty program.

1 (Rev. & Tax. Code, §§ 19732, subd. (e) & 19733, subd. (a)(3).) Appellant appears to concede that the
2 clear language of R&TC section 19732, subdivision (e), bars her claim for refund. Appellant's
3 argument that she should be entitled to a refund for such amounts because she erroneously made these
4 payments would render R&TC section 19732, subdivision (e), meaningless. According to appellant's
5 logic, the only taxpayers who should be subject to R&TC section 17932, subdivision (e), would be
6 those taxpayers who would not ultimately prevail in their claims for refund or credit. Staff notes that
7 appellant self-reported the \$622 penalty for early distribution of a qualified plan on her original 2001
8 return and voluntarily signed the amnesty application on March 8, 2005, which notified her she was
9 waiving her right to file a claim for refund or credit. Because R&TC section 19732, subdivision (e),
10 precludes a claim for refund or credit for any amount paid in connection with the tax amnesty program
11 it appears that the Board does not have jurisdiction to consider respondent's action in denying
12 appellant's claim for refund for amounts she paid through the tax amnesty program.

13 To the extent that appellant is making, or wishes to make, constitutional arguments, such
14 arguments may be made in the appropriate court of law or to the California Legislature. The Board is
15 precluded from determining the constitutional validity of California statutes, and has an established
16 policy of declining to consider constitutional issues. (Cal. Const., art. III, § 3.5; *Appeal of Aimor Corp.*,
17 83-SBE-221, Oct. 26, 1983; *Appeals of Walter R. Bailey*, 92-SBE-001, Feb. 20, 1992 (*Bailey*).)

18 Furthermore, the Board held in *Bailey*:

19 [D]ue process is satisfied with respect to tax matters so long as an
20 opportunity is given to question the validity of a tax at some stage of the
21 proceedings. It has long been held that more summary proceedings are
22 permitted in the field of taxation because taxes are the lifeblood of
23 government and their prompt collection is critical. [Citations omitted.]

24 Furthermore, this Board has determined that a taxpayer's disagreement with the law should be directed
25 to the Legislature, which is charged with formulating the law, rather than to those who are charged with
26 enforcing the law as it is written. (*Appeal of Thomas C. and Donna G. Albertson*, 84-SBE-002, Jan. 17,
27 1984; *Appeal of Chester A. Rowland*, 75-SBE-071, Oct. 21, 1975; *Appeal of Samuel R. and Eleanor H.*
28 *Walker*, 73-SBE-020, Mar. 27, 1973.)

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