

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: August 18, 2006

From: Kristine Cazadd
Chief Counsel 

Subject: **Board Meeting – August 29, 2006**
Chief Counsel Matters – Item J1

Status Report on Chapter 4, *Appeals from Actions of the Franchise Tax Board*, of the New Rules of Practice¹

I. Status and Future Recommendation

Staff has completed the fourth draft of Chapter 4, *Appeals from the Franchise Tax Board*, of the New Rules of Practice as provided in Attachment A, which shows the revisions in strikethrough and underline format, and Attachment B, which is identical but does not show the revisions. Chapter 4 is the result of a year long effort to compile the Board's current procedures and practices for handling appeals from the Franchise Tax Board (FTB);² refine those procedures to make them more efficient and understandable; address various procedural issues; and determine which practices are best suited to being promulgated as regulations. Staff will recommend chapter 4 for future adoption based on the following:

- Chapter 4 revisions are comprehensive without being overly detailed, flexible enough to adapt to unusual appeals, and clearly worded to avoid confusion;
- Chapter 4 will promote public confidence in the Board's procedures by clarifying taxpayers' equal access to appeals and maximizing the efficient use of the Board's and FTB's resources;
- Chapter 4 represents a general consensus among interested parties, Board staff, and the FTB; and
- Chapter 4 ensures that taxpayers have a plain, speedy and adequate remedy available to challenge FTB determinations as guaranteed by state and federal law.

II. New Practices and Procedures Incorporated into Chapter 4

In accordance with the projects goals and extensive discussion with interested parties, including the FTB, the following provisions are in the current draft of chapter 4:

¹ Staff is in the process of renaming the New Rules of Practice Board direction on April 18, 2006.

² The history and background regarding chapter 4 is provided in detail in Attachment C.

A. **Provisions that Slightly Change Current Practices**

- **Process for Reviewing Jurisdictional Issues.** Chapter 4 slightly modifies the Board's current practice for determining its jurisdiction to hear an appeal. Under current practice, the Board Proceedings Division (BPD) makes an initial determination of whether the Board has jurisdiction. If the Board clearly lacks jurisdiction, the appeal is dismissed. If the Board has jurisdiction, or if there is any question as to the Board's jurisdiction, the appeal is accepted and the briefing and decision process starts. Under chapter 4's proposed revision, when the BPD receives an appeal where the Board's jurisdiction is unclear, it will refer to the Chief Counsel for further investigation. If the Chief Counsel's investigation reveals that the Board clearly lacks jurisdiction, the appeal will be dismissed without devoting further time and resources. If, after the investigation, it is determined that the Board clearly has jurisdiction or there is still a jurisdictional question, the appeal will be accepted and the briefing process will commence. The parties will be expected to brief and argue any jurisdictional issues.
- **Perfecting Appeals.** The old Rules of Practice procedures giving taxpayers additional time to perfect an appeal if the initial filing lacks some essential information, are confusing to appellants. Chapter 4 clarifies the perfection procedure by creating a separate regulation addressing perfection, and requiring that appeals be perfected before briefing can begin, and specifying the information needed to perfect an appeal. Chapter 4 also permits the Chief of BPD to accept appeals that "substantially comply" with the requirements for a perfected appeal.
- **Amicus (Non-Party) Briefs.** The old Rules of Practice generally allow non-parties to file amicus briefs. Chapter 4 continues this practice, but prohibits individuals and entities from filing more than one amicus brief without permission in order to prevent a non-party from disrupting the process. Chapter 4 also gives the Appeals Division authority to request amicus briefs, whenever useful to expedite or resolve appeals.
- **Discretionary Supplemental Briefing.** The old Rules of Practice recognize that the standard briefing schedule may not always be adequate and allow the Appeals Division or the Board to request supplemental briefing. Chapter 4 expands this practice by allowing individual Board Members to request additional briefing through the Appeals Division, and also integrates supplemental briefing into the scheduling process by requiring that the Board Chair be notified whenever supplemental briefing is requested.
- **Requesting Oral Hearings.** Current procedures do not contain a deadline for taxpayers to request an oral hearing. Chapter 4 creates a deadline requiring taxpayers to request an oral hearing within 30 days after the conclusion of the briefing schedule, and permits the Chief Counsel to accept untimely requests if there is reasonable cause. The vast majority of taxpayers will not be affected by the new deadline, but the new procedures will conserve staff resources by preventing the preparation of about two dozen needless summary decisions each year.³

³ In the first six months of 2006, the Board decided 247 appeals from the FTB (not including petitions for rehearing) and 12 appeals involved late requests for oral hearings.

- **Scheduling Oral Hearings.** Under current practice, the BPD schedules and notices an oral hearing before the Appeals Division reviews the appeal file, which prevents the Appeals Division from requesting additional briefing and occasionally results in some appeals being sent to the Board with an incomplete record. Chapter 4 now requires that Appeals review the file before an appeal is scheduled for an oral hearing. If the Appeals Division determines that the file is incomplete, it may then request additional briefing or hold a pre-hearing conference (see below) to obtain additional information without disrupting the oral hearing calendar.⁴

B. Provisions that Significantly Change Current Practices

- **Innocent Spouse Briefing Schedule.** Recent statutory amendments require that both spouses be given meaningful participation in an innocent spouse appeal from the FTB (see Rev. & Tax. Code, § 18533, subd. (e)(3)(B), effective Jan. 1, 2004). Currently, there is no formal briefing schedule that accounts for having three adverse parties, and staff is temporarily treating both spouses as having filed separate appeals in order to provide both spouses with the opportunity to file briefs and request oral hearings. This temporary informal method for administering innocent spouse appeals has been awkward and confusing. Chapter 4 incorporates the lessons learned, and incorporates the interested parties' suggestions, and proposes a detailed briefing schedule for innocent spouse appeals. The new provisions give the non-appealing spouse⁵ the right to file an opening and reply brief; allow the other parties to respond to those briefs; allow either spouse to request an oral hearing, and allow the Board to hold a single hearing, (unless a court order prohibits both spouses from appearing or the Board Chair determines that a single hearing would be unsafe or disruptive).
- **Discretionary Pre-Hearing Conferences.** Currently, the old Rules of Practice do not provide appeals conferences in appeals from the FTB. Under the new rules, taxpayers and the FTB will be able to request a pre-hearing conference in those cases where they feel it is appropriate, and the Appeals Division will have the discretion to hold pre-hearing conferences when the appeal file is incomplete. The Board may also order the Appeals Division to hold pre-hearing conferences. If a pre-hearing conference would be unproductive and a misuse of resources, the Chief Counsel may deny a conference request. The new pre-hearing conferences will allow the Appeals Division, the parties, and the Board to more fully develop appropriate appeals, but should not lengthen the appeals process because pre-hearing conferences will always be held after briefing concludes, and normally before the oral hearing.

⁴ Based on a review of a small sample of recent cases staff believes that as many as one-third of the appeals scheduled for oral hearing would benefit from this slight change in procedure.

⁵ 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.

- **Criteria for Adopting Formal Opinions.** The Board does not currently have any criteria for the adoption of Formal Opinions. Based upon suggestions from the interested parties, chapter 4 would incorporate criteria from the California Rules of Court that govern the publication of appellate opinions. Those criteria are: 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 and FTB believe that these criteria will create a rational and consistent foundation for the adoption of Formal Opinions and still preserve the Board's discretion.
- **Criteria for Imposing Frivolous Appeal Penalties.** The Board does not currently have formal criteria for determining when to impose frivolous appeal penalties, or in what amount. Chapter 4 proposes several non-exclusive criteria based on experience and the comments of interested parties. These criteria include, but are not limited to: whether the taxpayer is making arguments that the Board or courts have repeatedly rejected; whether the taxpayer is making the same arguments that he or she unsuccessfully made in prior appeals; whether the taxpayer filed the appeal with the intent of delaying the legitimate collection of tax; 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, provide much-needed notice to taxpayers, and preserve the Board's current discretion.
- **New Procedures for Briefing and Decisions on Petitions for Rehearing.** The old Rules of Practice do not provide guidance on many of the current informal practices utilized in connection with petitions for rehearing. Based upon suggestions from interested parties, and to ensure the consistent treatment of similarly-situated taxpayers, chapter 4 proposes a step-by-step briefing and decision process for petitions for rehearing. Taxpayers and the FTB would still be required to file their petitions within 30 days after the Board's decision, but will have an additional 30 days to perfect timely, but incomplete petitions. Once a petition for rehearing is perfected, the non-filing party will be given an additional 30 days to respond before the Appeals Division prepares a decision on the petition and submits the decision to the Board as a non-appearance matter. If the Board grants a rehearing, the filing party will have 30 days to file an opening brief for the rehearing, the non-filing party will be given 30 days to reply, and the filing party will get an additional 30 days to respond to the non-filing party's reply brief, unless the Board determines that a different schedule would be more appropriate.

III. Recommendation

For these reasons, staff will be recommending that the Board adopt chapter 4, *Appeals from Actions of the Franchise Tax Board*, as proposed in Attachment A and Attachment B.

KC:jlh
Attachments

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Approved 
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