



BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeals of
GEORGE FRENCH, JR., and MARY E. FRENCH }

Appearances:

For Appellants: Frank C. Scott, Certified Public
Accountant

For Respondent: Cleo Gray, Junior Counsel

O P I N I O N

These appeals by George French, Jr., and Mary E. French are made pursuant to Section 19059 of the Revenue and Taxation Code from the action of the Franchise Tax Board in denying their claims for refund of personal income taxes in the amounts of \$3,161.79 for George French, Jr., and \$3,211.79 for Mary E. French for the year 1943.

Appellants, husband and wife, filed their tax returns for 1943 in March of 1944. Their 1943 taxes were therein computed to be \$9,323.02 for the husband and \$9,322.96 for the wife. The husband remitted \$2,337.29 and offset overpayments of tax in 1941 and 1942 in the amount of \$6,985.73. The wife remitted \$2,289.76 and offset overpayments of tax in 1941 and 1942 in the amount of \$7,033.20. Claims for refund of the overpayments were filed with the returns,

The overpayments were due to the mistaken inclusion in income for 1941 and 1942 of receipts from a transaction which should not have been reported until 1943. Their accountant stated on their returns the reason for taking this action: "In view of the precise interrelation of the claimed overpayments for 1941 and 1942 to the taxes computed according to the provisions of Section 7.1 for 1943 and the inhibition by the Personal Income Tax Act of the allowance of interest on overpayments of this character [until 1949, Section 20 of the Act, later Section 19062 of the Code, did not allow interest on overpayments made through mistake of the taxpayer] as well as the size of the overpayments involved, I have taken the liberty of suggesting to the taxpayers the remittance only of the net differences between the overpayments and the total taxes on their 1943 returns, which differences are in each case less than one-third of the 1943 tax." In 1945 each made an overpayment of \$61.79 and on March 3, 1952, they paid \$3,100 and \$3,150, respectively, to protect themselves against

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the running of interest in the event that it was determined that additional tax was due for the year 1943. The Franchise Tax Board credited these sums to the Appellants' accounts for 1943.

In June of 1953, after a Federal determination of the issues involved concerning the income years 1941, 1942 and 1943, the Franchise Tax Board approved the claims for refund for 1941 and 1942. In November, 1953, after the State Board of Control had approved the refunds, the Franchise Tax Board credited sufficient amounts of the overpayments for those years to extinguish what it regarded as the unpaid balances of the 1943 liabilities and paid the remainder to the Appellants. The Franchise Tax Board regarded its credit of the approved claims for refund as for the first time discharging the 1943 liabilities. As a result, interest was charged against husband and wife in the amounts of \$3,173.43 and \$3,195.62, respectively,

The Appellants contend that they are entitled to refunds of the amounts overpaid in 1945 and the amounts paid in 1952 on the ground that the 1943 tax was extinguished in 1944 by the cash payments then made plus the offsets claimed for overpayments in 1941 and 1942.

The Franchise Tax Board argues that the Appellants could **not**, on their own initiative, credit the earlier overpayments **against** the later liability and point to Section 20 of the Personal Income Tax Act (now Sections 19051 and 19052 of the Revenue and Taxation Code), which read:

"If, in the opinion of the commissioner, or the State board, as the case may be, there has been an overpayment of tax, penalty or interest by a taxpayer for any year for any reason, the amount of such overpayment shall be credited against any taxes then due from the taxpayer under this act, and the balance refunded to the taxpayer. No such credit or refund shall be allowed or made until approved by the State Board of Control... ."

It **points** out further that such action would be in direct conflict with its Regulation Article 20-1 (now subparagraph (8) of Personal Income Tax Regulation 19051-19062) which read:

"Taxpayers may not on their own initiative offset an overpayment for one year or in one installment against taxes **due** for another year or in another installment. The full amount of the tax or any in-

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stallment thereof for each year must be paid, notwithstanding that an overpayment may have been made, unless the taxpayer has filed a claim for refund of the overpayment and has been notified that the overpayment has been credited on the tax or installment due."

Appellants contend that this regulation is invalid, that Section 15(d)(2) of the Personal Income Tax Act (now Section 18691 of the Revenue and Taxation Code) supports their position, and that in any event they are supported by the doctrine of equitable recoupment. We are unable to agree with any of these contentions,

The argument that the regulation is invalid seems to us obviously unsound. Appellants allege that it "does not interpret and is not based on any identifiable statutory provision." We think that a reasonable interpretation of Section 20, supra, requires the conclusion that either the Commissioner (or his successor, the Franchise Tax Board) or this Board must determine that an overpayment of tax has been made, and that the State Board of Control must approve, before the amount of the overpayment may be credited or refunded to the taxpayer. The above quoted regulation is nothing more than a statement that the unilateral action of the taxpayer in taking the credit is not the equivalent of that procedure.

Section 15(d)(2) of the Personal Income Tax Act provided:

"When the correction of an erroneous inclusion or deduction of an item in the computation of income of any year results in an overpayment for one year and a deficiency for another year, the overpayment, if the period within which credit for the overpayment may be allowed has not expired, shall be credited on the deficiency, if the period within which the deficiency may be proposed has not expired, and the balance, if any, shall be credited or refunded as provided in Section 20. No interest shall be assessed on such portion of the deficiency as is extinguished by the credit for the period of time subsequent to the date the overpayment was made."

This section is not appropriate to the situation here presented. There were no deficiencies for the year 1943 resulting from corrections by the Appellants or by the Franchise Tax Board. The underpayments for 1943 resulted from the attempt of the Appellants, in direct conflict with the above-quoted regulation, to offset their overpayments against their self-assessed

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liabilities for that year, Appellants, however, argue that the principle of the section should be given precedence over technicalities, The short answer to this suggestion is that such an extension of the section would nullify the provision disallowing interest on overpayments which are due to the mistake of the taxpayer, Furthermore, to permit taxpayers to offset alleged but unproved overpayments against their current tax liabilities would create chaos in the collection of taxes.

Appellants' reliance upon the doctrine of equitable recoupment is, we feel, similarly misplaced. The cases cited in support of their contention, Bull v. United States, 295 U. S. 247, and Stone v. White, 301 U. S. 532, deal with tax liabilities barred by the statute of limitations and have no application in these appeals. Appellants' claims for refund for 1941 and 1942 were not barred and adequate affirmative remedies were available to them. We conclude, accordingly, that the Franchise Tax Board's action must be upheld.

O F D E R

Pursuant to the views expressed in the Opinion of the Board on file in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to Section 19060 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the claims for refund of personal income taxes in the amounts of \$3,161.79 by George French, Jr., and \$3,211.79 by Mary E. French for the year 1943, be and the same is hereby sustained.

Done at Sacramento, California, this 16th day of December, 1958, by the State Board of Equalization.

George R. Reilly _____, Chairman

Paul R. Leake _____, Member

J. H. Quinn _____, Member

Robert E. McDavid _____, Member

Robert G. Kirkwood _____, Member

ATTEST: Dixwell L. Pierce Secretary