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10 **BOARD OF EQUALIZATION**  
 11 **STATE OF CALIFORNIA**

12 In the Matter of the Appeal of: ) **HEARING SUMMARY**  
 13 ) **PERSONAL INCOME TAX APPEAL<sup>2</sup>**  
 14 ) **DOUGLAS GAIL HUFNAGEL AND** ) Case No. 510017  
 15 ) **ROBYN HUFNAGEL<sup>1</sup>** )

<u>Years</u>	<u>Claims For Refund</u>
1995	\$8,496.88
1996	\$14,131.43 <sup>3</sup>
1997	\$8,668.22 <sup>4</sup>
1999	\$1,234.00
2000	\$5,311.00

21 <sup>1</sup> Appellants reside in Shasta County, California.

22 <sup>2</sup> This appeal was postponed from the September 14, 2010, Board calendar at appellants' representative's request and  
 23 recalendared to the December 14-16, 2010, Board calendar.

24 <sup>3</sup> During this appeal, respondent obtained federal Individual Master Files (IMF's), which support that for 1996 and 1997, the  
 25 IRS made federal changes and appellant-husband's claims for refunds were timely within the 2-year statute of limitation  
 26 pursuant to Revenue and Taxation Code section 19311. Respondent refunded \$14,131.43, plus accrued interest of \$8,820.34,  
 27 for a total payment of \$22,951.77, to appellants on April 20, 2010. Thus, tax year 1996 is no longer at issue in this appeal.

28 <sup>4</sup> Appellant-husband's amended return for 1997 reduced his federal AGI from \$139,316 to \$86,034 and did not claim a  
 refund due. Respondent accepted the amended return and reduced the underpayment penalty from \$553.95 to 231.50,  
 resulting in an overpayment amount of \$8,668.22. Respondent transferred credit amounts of \$572.03 and \$5,308.12 to  
 appellant-husband's tax liabilities for 2003 and 2005, and refunded the remaining 1997 overpayment of \$7,430.57, plus  
 accrued interest of \$2,228.77 to appellant-husband on April 20, 2010. Thus, it appears tax year 1997 is no longer at issue in  
 this appeal.

Appeal of Douglas Gail Hufnagel  
 and Robyn Hufnagel

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1 Representing the Parties:

2  
3 For Appellants: Dale A. Hoppes, Certified Public Accountant

4 For Franchise Tax Board: Suzanne L. Small, Tax Counsel III

5  
6 QUESTION: Whether appellants' claims for refund are barred by the statute of limitations.

7 HEARING SUMMARY

8 Facts

9 1995

10 Appellants filed their 1995 tax return using the married filing joint status on or about  
11 October 15, 1996. (Resp. Op. Br., exhibit A.) Appellants return reported a California adjusted gross  
12 income (AGI) of \$135,652, itemized deductions of \$16,696, a self-assessed total tax liability of \$7,562,  
13 and \$5,420 in estimated tax payments. (*Id.* at exhibit B.) Respondent accepted the self-assessed tax  
14 liability, but only allowed credits for \$2,180 in extension payments according to its records, leaving an  
15 outstanding balance of \$5,382. Based on the underpayment, respondent imposed an estimated tax  
16 penalty of \$264.26 and underpayment penalty of \$269.10, and issued appellants a letter notifying them  
17 of the outstanding balance on October 31, 1996. Appellants fully paid their tax liability with a payment  
18 of \$6,581.16 on or about January 21, 1997. (*Id.* at exhibit C, lines 3-7.)

19 Appellants filed an amended return on or about May 31, 2005,<sup>5</sup> claiming a reduction in  
20 their federal AGI from \$134,478 to \$30,167, calculating a self-assessed tax of zero dollars, and claiming  
21 a refund in the amount of \$5,043.<sup>6</sup> (Resp. Op. Br., exhibit D.) Respondent accepted the self-assessed  
22 tax amount and abated the underpayment penalty, resulting in an overpayment amount of \$8,496.88.  
23 Respondent issued a statement of account to appellant-husband dated July 30, 2007, explaining there  
24 was an overpayment for the 1995 tax year, but the amount could not be refunded because the statute of  
25

26  
27 <sup>5</sup> Respondent notes that the district office's received date stamped on the returns for all five years bear a 2004 date, but the  
28 returns were not signed until May 31, 2005, and respondent's records also reflect the 2005 date. Neither party asserts the  
returns were actually filed in 2004.

<sup>6</sup> Respondent notes appellants filed a second copy of the returns for each of the five tax years on or about August 15, 2005.

1 limitations expired. (Appeal Letter attachments.) This timely appeal followed.

2 1999

3 Appellant-husband filed his 1999 tax return using the head of household status on or  
4 about May 31, 2005. (Resp. Op. Br., exhibit O.) Appellant-husband's return reported a California AGI  
5 of \$91,994, itemized deductions of \$6,940, and a self-assessed total tax liability of \$4,506, and estimated  
6 tax payments of \$5,740. (*Id.* at exhibit P.) Respondent accepted the self-assessed tax liability, resulting  
7 in an overpayment of \$1,234. (*Id.* at exhibit Q.) Respondent issued a statement of account to appellant-  
8 husband dated July 30, 2007, explaining there was an overpayment for the 1999 tax year, but the amount  
9 could not be refunded because the statute of limitations expired. (Appeal Letter attachments.) This  
10 timely appeal followed.

11 2000

12 Appellant-husband filed his 2000 tax return using the head of household status on or  
13 about May 31, 2005. (Resp. Op. Br., exhibit O.) Appellant-husband's return reported a California AGI  
14 of \$58,658, itemized deductions of \$8,893, and a self-assessed total tax liability of \$1,098, and estimated  
15 tax payments of \$5,900. (*Id.* at exhibit R.) Respondent accepted the self-assessed tax liability, resulting  
16 in an overpayment of \$5,311. (*Id.* at exhibit S.) Respondent issued a statement of account to appellant-  
17 husband dated July 30, 2007, explaining there was an overpayment for the 2000 tax year, but the amount  
18 could not be refunded because the statute of limitations expired. (Appeal Letter attachments.) This  
19 timely appeal followed.

20 Contentions

21 Appellants contend that their claims for refund, in the form of amended and original  
22 returns for the years at issue, qualify as claims for refund pursuant to Revenue and Taxation Code  
23 (R&TC) section 19307 and California Code of Regulations, title 18, section (Regulation) 19322, and  
24 should be accepted as timely under (R&TC) sections 19307, 19311, 19314, 19323, and the doctrine of  
25 equitable recoupment. Appellants assert the date to use for determining if the claims are timely under  
26 the statute of limitations should be the date the returns were received and accepted by respondent.  
27 (Appeal Letter, p. 2.) Appellants contend the overpayments from the years at issue should have been  
28 immediately applied to offset remaining liability for other years when respondent accepted the returns.

Appeal of Douglas Gail Hufnagel  
and Robyn Hufnagel

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1 Appellants assert they never received notice that their claims were denied, which respondent was  
2 required to send under R&TC section 19323.<sup>7</sup> Appellants state they made several attempts to contact  
3 respondent regarding this issue, by mail, fax, and phone, but did not receive prompt or accurate  
4 assistance at any time. (*Id.* at p. 3.)

5 Appellants explain that they discovered in 1999 that the accounting records for the  
6 previous several years contained errors which appeared to be an intentional effort (by the accountant(s)  
7 at the time) to make the business look more profitable. (Appeal Letter, p. 1.) Appellants indicate that  
8 his new accountant recommended not filing tax returns for 1998, 1999, and 2000 until all the errors  
9 could be corrected, and that further delays from accountants led to the filing date on or about May 31,  
10 2005. It appears appellants contend this constitutes fraud that prohibited them from filing original  
11 returns correctly and timely. Appellants state they will provide further evidence of both fraud and  
12 double taxation in support of their equitable recoupment claim at the hearing, but do not elaborate on  
13 these contentions. (App. Reply Br.)

14 Appellants indicate respondent has conceded the refunds for tax years 1996 and 1997 for  
15 \$14,131.43 and \$8,668.22, respectively, but asserted respondent erred in not immediately issuing the  
16 refund for those years. (App. Reply Br.) Respondent, noting that it usually does not issue refunds for  
17 years that are still on appeal before the board, has since issued refunds for 1996 and 1997 to appellant-  
18 husband on April 20, 2010. (See footnotes three and four herein.) Appellants contend the Internal  
19 Revenue Service (IRS) accepted appellant-husband's returns for 1999 and 2000 as part of a larger audit,  
20 allowed credit of overpaid amounts, and respondent should similarly issue refunds for these years  
21 immediately. (*Id.* at p. 2.)

22 Respondent contends appellants' claims for refund for the 1995, 1999, and 2000 years are  
23 barred by the statute of limitations under R&TC section 19306. Respondent asserts R&TC section  
24 19307 does not provide an extension to the limitations on refunds and credits under section 19306.

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26 <sup>7</sup> Although appellants make this claim in the appeal letter documents dated August 19, 2009, they included as an attachment  
27 to their appeal letter correspondence from respondent dated July 30, 2007, stating that the overpayment amounts for the years  
28 at issue are outside of the statute of limitations and therefore will not be refunded. Respondent notes that if it fails to act on a  
claim for refund within six months of filing that claim, the claim is deemed denied and appellants may appeal to this Board.  
(Resp. Op. Br., p. 10; Rev. & Tax. Code, § 19331.)

1 Respondent states R&TC section 19311 allows a taxpayer to file a claim for refund within two years of a  
2 change made by the IRS that results in a refund or credit as well as a corresponding refund claim under  
3 California law. (Resp. Op. Br., p. 8.) Respondent contends appellants' refund claims for 1995, 1999,  
4 and 2000 can not be allowed under R&TC section 19311. Respondent likewise contends appellants'  
5 claims for refund for 1995, 1999, and 2000 are not allowed under R&TC section 19314. Respondent  
6 asserts the doctrine of equitable recoupment is narrowly limited by case law, and appellants have failed  
7 to show there was a single transaction that was subject to taxation on inconsistent legal theories, as  
8 required to allow a refund under the doctrine. (Resp. Op. Br., p. 11.)

9 Respondent asserts appellants' IRS account transcripts for 1999 and 2000 do not establish  
10 the IRS allowed claims for refunds for those years. Instead, respondent contends, the transcripts show  
11 only estimated tax payments and declarations, verification of a power of attorney, penalties, and  
12 payments applied to the tax year. (Resp. Reply Br., p. 1.)

### 13 Applicable Law

14 The general statute of limitations for filing a refund claim is set forth in R&TC section  
15 19306. Under that section, the last day to file a claim for refund is the later of:

- 16 1. Four years from the date the return was filed, if filed within the extended due date;
- 17 2. Four years from the due date of the return, without regard to extensions; or
- 18 3. One year from the date of the overpayment.

19 Withholding payments are deemed paid on the last day prescribed for filing the return pursuant to  
20 R&TC section 19002, subdivision (c)(1).

21 The language of the statute of limitations is explicit and must be strictly construed.  
22 (*Appeal of Michael and Antha L. Avril*, 78-SBE-072, Aug. 15, 1978.) The statute of limitations is  
23 "strictly construed and . . . a taxpayer's failure to file a claim for refund, for whatever reason, within the  
24 statutory period bars him from doing so at a later date." (*Appeal of Earl and Marion Matthiessen*, 85-  
25 SBE-077, July 30, 1985.) It is a taxpayer's responsibility to file a claim for refund within the timeframe  
26 prescribed by law. (*Appeal of Earl and Marion Matthiessen, supra.*) Federal courts have stated that  
27 fixed deadlines may appear harsh because they can be missed, but the resulting occasional harshness is  
28 redeemed by the clarity of the legal obligation imparted. (*Prussner v. United States* (7th Cir. 1990)  
896 F.2d 218, 222-223; *United States v. Locke* (1985) 471 U.S. 84; *United States v. Boyle* (1985) 469

Appeal of Douglas Gail Hufnagel  
and Robyn Hufnagel

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1 U.S. 241, 249].)

2 R&TC section 19316 contains the only exception to the statute of limitations under  
3 California law. R&TC section 19316 tolls the statute of limitations during a period of “financial  
4 disability,” meaning the taxpayer was unable to manage his or her financial affairs due to a medically  
5 determinable physical or mental impairment that is expected to be a terminal impairment or is expected  
6 to last for a continuous period of not less than 12 months. (Rev. & Tax. Code, § 19316, subd. (b)(1).)  
7 In order to demonstrate the existence of a financial disability, a taxpayer must submit a signed affidavit  
8 from a physician that explains the nature and duration of the taxpayer’s physical or mental impairments.  
9 (*Appeal of James C. and Florence Meek*, 2006-SBE-001, Mar. 28, 2006.) In addition, the taxpayer must  
10 show that he satisfies the strict definition of “financial disability” such that the taxpayer could not  
11 manage his or her financial affairs; it is not sufficient to show that the taxpayer could not engage in a  
12 regular occupation. (*Ibid.*)

13 This Board has held that the FTB has no duty to discover an overpayment made by a  
14 taxpayer (*Appeal of Manuel and Ofelia C. Cervantes*, 74-SBE-029, Aug. 1, 1974); nor does the FTB  
15 have a duty to inform a taxpayer of the time within which a claim for refund must be filed in order to  
16 avoid application of the statute of limitations. (*Appeal of Earl and Marion Matthiessen, supra.*)

17 With respect to federal adjustments that result in a credit or refund, a claim for such  
18 credit or refund may be filed within two years from the date of the final federal determination as defined  
19 in R&TC section 18622 or within the period provided in R&TC section 19306, 19307, 19308 or 19316,  
20 whichever period expires later. (Rev. & Tax. Code, § 19311, subd. (a).) Similarly, respondent is  
21 authorized to allow a credit, make a refund or mail a notice of proposed overpayment resulting from a  
22 final federal determination within the later of (1) two years from the date of the final federal  
23 determination or (2) within the period provided in R&TC section 19306, 19307, 19308 or 19316.  
24 (Rev. & Tax. Code, § 19311, subd. (a)(2).)

25 R&TC section 19307 provides that, for purposes of section 19306, a return filed within  
26 four years from the last day prescribed for filing the return showing withholding credits or estimated tax  
27 paid pursuant to section 19032, 19024, or 19136, in excess of the tax due shall be considered a claim for  
28 refund of the excess (if more than \$1).

Appeal of Douglas Gail Hufnagel  
and Robyn Hufnagel

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1 R&TC section 19308 provides that the period within which a claim for credit or refund  
2 may be filed (or allowed), is the period within which respondent may mail a notice of proposed  
3 deficiency assessment under the same circumstances if: (1) the taxpayer has signed a waiver extending  
4 the period within which respondent may propose a deficiency assessment; or (2) the taxpayer has signed  
5 a federal waiver (or renewals thereof) for the period for proposing and assessing federal deficiencies.

6 R&TC section 19323 provides that if respondent disallows a claim for refund, it shall  
7 notify the taxpayer and provide an explanation for the disallowance.

8 R&TC section 19314 provides that certain overpayments may be used to offset a  
9 deficiency for the same or another year. Subdivision (c) of that section further provides that “[n]o  
10 refund shall be allowed under subdivision (a) unless before the period set forth in Section 19306 a claim  
11 therefore is filed by the taxpayer or unless before the expiration of that period the Franchise Tax Board  
12 has allowed a credit or made a refund.”

13 The application of the doctrine of equitable recoupment has been limited to situations  
14 wherein a fund of money arising from a single transaction or taxable event has been subjected to tax  
15 twice on inconsistent legal theories. In such event, what was mistakenly paid may be recouped against  
16 what is correctly due. (*Bull v. United States* (1935) 295 U.S. 247, 261; *Stone v. White* (1937) 301 U.S.  
17 532; *Rothensies v. Electric Storage Battery Co.* (1946) 329 U.S. 296, 300; *Appeal of Estate of*  
18 *Zebulon P. Owings, Deceased, and Mabel J. Owings*, 75-SBE- 008, Jan. 7, 1975.) Further, an  
19 underlying inquiry in determining the applicability of the doctrine in favor of the taxpayer is whether  
20 the government received monies which in equity and good conscience belong to the taxpayer.  
21 (*Bull v. United States*, supra at 260; *Boyle v. United States* (3d Cir. 1965) 355 F.2d 233.) However,  
22 equitable recoupment is to be applied narrowly so as not to seriously undermine the statute of  
23 limitations in tax matters. (*Rothensies v. Electric Storage Battery Co.*, supra at 303.) The Board has  
24 determined that it has the authority to apply the doctrine in an appropriate situation. (*Appeals of*  
25 *Wilford and Gertrude Winkenbach, et al.*, 75-SBE-081, Dec. 16, 1975.)

26 The doctrine of equitable recoupment is only applicable where “a single transaction  
27 constitute[s] the taxable event claimed upon and the one considered in recoupment.”  
28 (*Rothensies v. Electric Storage Battery Co.*, supra, 329 U.S. at 299; see also *O'Brien v. United States*

1 (7th Cir. 1985) 766 F.2d 1038.) A threshold requirement of the doctrine is that it may not be used “to  
2 revive an untimely affirmative refund claim, as opposed to offset[ing] a timely government claim of  
3 deficiency with a barred claim of the taxpayer.” (*O'Brien v. United States*, supra, 766 F.2d at 1049.) In  
4 the *Appeal of Frank and Elsie M. Bartlett* (74-SBE-019), decided on May 15, 1974, appellants argued  
5 that the Board should apply the doctrine to compel respondent to offset a tax overpayment made in 1963  
6 against a 1969 deficiency when the statute of limitations for filing a claim for refund expired. There, the  
7 Board held that the doctrine was inapplicable because “the items of income were not derived from a  
8 single transaction” in that “the declaration and payment of dividends for each year constituted a single  
9 and separate transaction” and “the tax was applied on the basis of income received in each taxable year.”  
10 In *Appeal of James T. King* (64-SBE-077), decided October 27, 1964, this Board stated receipts of  
11 income in earlier years which give rise to alleged overpayments constitute separate, distinct taxable  
12 events, and not a single transaction.

### 13 STAFF COMMENTS

14           Respondent has agreed that appellants 1996 and 1997 claims were timely. The parties  
15 should next be prepared to discuss whether appellants' claims for refund for 1995, 1999, and 2000 were  
16 timely. According to the evidence thus far provided, it appears as though appellants' claims for refund  
17 for these years, filed May 31, 2005, are barred by the statute of limitations pursuant to R&TC section  
18 19306. Thus, with respect to the four-year statute of limitations, it appears that the claims for refund  
19 were all filed more than four years from the due dates of the 1995, 1999, and 2000 returns (October 15,  
20 1996, April 15, 2000, and April 15, 2001, respectively). With respect to the one-year statute of  
21 limitations, payments for each of the years were either timely extension payments (for the 1999 and  
22 2000 tax years) made on April 15, 2000 and April 15, 2001, respectively, or payment made January 21,  
23 1997 (for the 1995 tax year). Accordingly, the May 31, 2005, refund claims were filed outside the one-  
24 year statute of limitations. It further appears from the federal account transcripts provided by appellants  
25 that the claims for refund for these years are not considered timely under the statute of limitations  
26 provided for in R&TC section 19311, because no such federal change abating tax or allowing any  
27 credits or refunds appears to be shown. Appellants should be prepared to provide any documentation  
28 they have that indicates any federal change was made to appellants' 1995, 1999, or 2000 tax years.

Appeal of Douglas Gail Hufnagel  
and Robyn Hufnagel

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1 Appellants have made a bare assertion that the doctrine of equitable recoupment is  
2 applicable. At the hearing, appellants should be prepared to elaborate on their argument for some form  
3 of equitable recoupment and to provide supporting case law or other authority applying that form of  
4 equitable relief to facts similar to those presented here. Appellants state they will provide documents  
5 and evidence to show that items of income have been subjected to tax twice, as well as evidence of fraud  
6 which prohibited them from filing their original returns correctly. (App. Reply Br.) Pursuant to  
7 California Code of Regulations, title 18, section 5523.6, if either party wants to provide additional  
8 evidence to the Board, that party should submit the additional evidence to Board Proceedings at least 14  
9 days prior to the oral hearing in this matter.<sup>8</sup>

10 In the briefing, appellants stated that the lack of information provided by respondent  
11 leaves them uncertain as to the exact amount they have overpaid their taxes. Should the Board  
12 determine that, in addition to the amounts already conceded by FTB regarding the 1996 and 1997 tax  
13 years, part or all of the amounts claimed should be refunded, both parties should be prepared to discuss  
14 the amounts received and collected by respondent for the years at issue, and what the total refund should  
15 be for each year at issue, including interest. Respondent has provided a chart of payments, penalties,  
16 and balances in its additional information dated September 9, 2010, including the refund amounts it  
17 issued for the 1996 and 1997 tax years.

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21 Hufnagel\_jj

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28 <sup>8</sup> Evidence exhibits should be sent to: Claudia Madrigal, Appeals Analyst, Board Proceedings Division, State Board of  
Equalization, P.O. Box 942879 MIC:80, Sacramento, California, 94279-0080.

Appeal of Douglas Gail Hufnagel  
and Robyn Hufnagel