OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

In the Matter of the Appeal of: **MILLENNIUM DENTAL TECHNOLOGIES, INC.**	OTA Case No. 18063362 Date Issued: May 31, 2019

OPINION

Representing the Parties:

For Appellant: Robert K. Morrow, J.D., LL.M.

For Respondent: Christopher M. Cook, Tax Counsel

For Office of Tax Appeals: Linda Frenklak, Tax Counsel IV

K. GAST, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19324, Millennium Dental Technologies, Inc. (appellant) appeals an action by respondent Franchise Tax Board (FTB) in denying appellant's claim for refund of $116,445, plus interest, and an installment payment program fee,[1] for the 2008 tax year. Appellant waived its right to an oral hearing. Therefore, the matter is being decided based on the written record.

ISSUE

Whether appellant's claim for refund is barred by the doctrine of res judicata, and if not, whether it is entitled to defer recognition of income from certain inventory sales to 2009.

FACTUAL FINDINGS

1. During the tax year at issue, appellant, taxed as a C corporation, manufactured and sold patented surgical laser dental equipment to dentists in California under written sales agreements.
2. After appellant filed its 2008 California corporation tax return (Form 100), FTB conducted an audit of that return. FTB determined that appellant had incorrectly deferred

[1] Appellant also requests a refund of penalties paid, but does not specify what penalties it is referring to. Rather, the limited record only indicates that it paid tax, interest, and an installment payment program fee.

to the 2009 tax year income from certain "sales not complete" transactions that occurred in the last 60 days of appellant's 2008 tax year. FTB thus increased appellant's 2008 taxable income by $1,039,270 from these transactions. This adjustment also resulted in the denial of claimed net operating losses (NOLs) because appellant's taxable income exceeded the income threshold for deducting such NOLs in 2008.

3. Based on its audit results, FTB issued a Notice of Proposed Assessment (NPA), proposing additional tax of $116,445, plus interest.
4. Appellant protested the NPA, but FTB subsequently issued a Notice of Action (NOA), affirming it.
5. Appellant appealed the NOA to the Board of Equalization (BOE), the predecessor to the Office of Tax Appeals (OTA), in a matter entitled *Appeal of Millennium Dental Technologies, Inc.*, Case No. 747501. Following a hearing, the BOE sustained FTB's proposed assessment on the merits, which was memorialized in a Notice of Board of Equalization Determination. It also denied appellant's petition for rehearing.
6. Appellant and FTB subsequently entered into an installment payment agreement. Under that agreement, appellant fully paid, in installments, the tax liability of $116,445, plus interest, and an installment payment program fee.
7. Appellant then filed a refund claim for the total amount paid for 2008, reasserting, as it did before the BOE, that its method of accounting for its income tax reporting was correct as filed and that it "remains convinced . . . the FTB's assessment . . . is in error."
8. FTB denied the refund claim, essentially stating that the BOE had already affirmed the 2008 NOA and denied appellant's petition for rehearing.
9. This timely appeal to OTA followed.

DISCUSSION

FTB argues that appellant's refund claim on appeal to OTA is barred by the doctrine of res judicata. It asserts appellant appeals the same issue upon which a final judgment has already been rendered by the BOE in a previous action brought by appellant against FTB. Appellant, on the other hand, did not address the issue of res judicata raised by FTB, even though OTA provided it with an opportunity to do so. Rather, appellant only discusses the income deferral issue, contending that, contrary to both FTB's and BOE's determinations, it properly deferred and recognized its income from sales of certain inventory in 2009, not 2008.

R&TC section 19802(a), provides that "[i]n the determination of any case arising under this part [e.g., when the BOE renders a final decision under R&TC section 19048], the rule of res judicata is applicable only if the liability involved is for the same year as was involved in another case previously determined." The doctrine of res judicata, or claim preclusion, is an affirmative defense developed by the courts to bar repetitious suits on the same cause of action, and it is applicable to tax litigation.[2] (*Commissioner v. Sunnen* (1948) 333 U.S. 591, 597 (*Sunnen*).) "Income taxes are levied on an annual basis. Each year is the origin of a new liability and of a separate cause of action. Thus if a claim of liability or non-liability relating to a particular tax year is litigated, a judgment on the merits is res judicata as to any subsequent proceeding involving the same claim and the same tax year." (*Id.* at p. 598.) In the administrative appeals context, the BOE has applied the basic premise of the doctrine, rejecting a taxpayer's appeal of a refund claim after the BOE ruled against it in a prior deficiency appeal dealing with the same tax year, liability, issue, facts, and arguments. (See, e.g., *Appeals of Williams, et al.* (84-SBE-050) 1984 WL 16129.)

The application of res judicata depends upon the satisfaction of four elements: (1) the parties in each action must be identical (or at least be in privity); (2) a court of competent jurisdiction must have rendered the first judgment; (3) the prior action must have resulted in a final judgment on the merits; and (4) the same cause of action or claim must be involved in both suits (or, here, appeals). (See *Sunnen*, *supra*, 333 U.S. at p. 597-598; see also *Koprowski*, *supra*, 138 T.C. at p. 62.) We conclude all four elements are satisfied in this case.

The first element is met because the parties in the current appeal before OTA and the prior appeal before the BOE (i.e., appellant and FTB) are identical. The second element is met because, under R&TC sections 19045 and 19047, the BOE had jurisdiction to hear appellant's timely appeal of FTB's NOA, and it rendered the first judgment. The third element is met because the BOE issued a final judgment on the merits in the prior appeal. It not only sustained FTB's proposed assessment on the merits, which was memorialized in a Notice of Board of Equalization Determination, but it also subsequently denied appellant's petition for rehearing. (R&TC, § 19048; Cal. Code Regs., tit. 18, § 5463(c)(2).) Finally, the fourth element is met

[2] That doctrine should be distinguished from the doctrine of collateral estoppel, or issue preclusion, which prevents the relitigation of an issue that has been previously litigated between the parties in one controversy but that recurs in other litigation between them in different controversies. (See *Koprowski v. Commissioner* (2012) 138 T.C. 54, 60 (*Koprowski*).)

because appellant's refund claim for the 2008 tax year involves the same cause of action—i.e., same tax year, issue, and liability—that the BOE decided and rejected on the merits. (See *Sunnen, supra*, 333 U.S. at p. 598 [each tax year is a separate cause of action].) Therefore, all four elements of res judicata have been met, and under R&TC section 19802(a), appellant is barred from bringing this refund claim.[3]

HOLDING

Appellant's refund claim is barred by the doctrine of res judicata. Accordingly, we do not need to reach the second issue of whether appellant is entitled to defer recognition of income from certain inventory sales to 2009.[4]

DISPOSITION

FTB's action is sustained in full.

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Kenneth Gast
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Kenneth Gast
Administrative Law Judge

We concur:

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Teresa A. Stanley
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Teresa A. Stanley
Administrative Law Judge

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Richard Tay
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Richard Tay
Administrative Law Judge

[3] Although "[i]n rare circumstances, a final judgment may be denied claim preclusive effect when to do so would result in manifest injustice," *F.E.V. v. City of Anaheim* (2017) 15 Cal.App.5th 462, 465, appellant made no such showing here.

[4] We do not need to address the interest and installment payment program fee included in appellant's refund claim, because it is not disputing whether those amounts were properly imposed or computed.