

**OFFICE OF TAX APPEALS**  
**STATE OF CALIFORNIA**

In the Matter of the Appeal of: ) OTA Case No. 18011019  
**MARTIN M. DEASY** )  
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**OPINION ON PETITION FOR REHEARING**

Representing the Parties:

For Appellant: Martin M. Deasy

For Respondent: Michael Cornez, Tax Counsel V

For Office of Tax Appeals: Tom Hudson, Tax Counsel III

T. STANLEY, Administrative Law Judge: On March 27, 2019, this panel issued an opinion regarding appellant Martin M. Deasy's proposed tax liability for 2014, which was reduced from \$16,850 to \$1,598 after concessions by the Franchise Tax Board (FTB). Our decision sustained the late-filing penalty and the filing enforcement cost recovery fee but abated the demand penalty finding that it was incorrectly applied. FTB filed a timely petition for rehearing, in accordance with California Revenue and Taxation Code (R&TC) section 19048, disputing only the demand penalty. Upon consideration of the petition, we conclude that the grounds set forth therein do not constitute good cause for a new hearing, in accordance with the Office of Tax Appeals Rules for Tax Appeals (Cal. Code Regs., tit. 18 (CCR), § 30604) and *Appeal of Do*, 2018-OTA-002P.

A rehearing may be granted where one of the following grounds exists, and the substantial rights of the complaining party are materially affected: (1) an irregularity in the appeal proceedings which occurred prior to the issuance of the written opinion and prevented fair consideration of the appeal; (2) an accident or surprise which occurred during the appeal proceedings and prior to the issuance of the written opinion, which ordinary caution could not have prevented; (3) newly discovered, relevant evidence, which the party could not have

reasonably discovered and provided prior to the issuance of the written opinion; (4) insufficient evidence to justify the written opinion or the opinion is contrary to law; or (5) an error in law. (CCR, § 30604(a)-(e); see also *Appeal of Do, supra.*)

In its petition for rehearing, FTB asserts that the opinion was against law or contrary to law regarding the application of CCR section 19133 (the Regulation). FTB asserts that our opinion relied on and applied an incorrect legal definition of the term “regulation,” and that we applied “erroneous rules of regulatory construction” to interpret the Regulation. FTB further asserts that the opinion improperly rejected FTB’s “long-standing interpretation and application” of the Regulation. Specifically, FTB argues that our decision “applied a literal reading of paragraph (2) of subdivision (b) that is inconsistent with Example (2) of subdivision (d) of the Regulation, and clearly inconsistent with [FTB’s] intent and interpretation of the Regulation.” FTB contends that if the decision had concluded that Example 2 was regulatory, the decision would have also concluded that the Regulation, as a whole, was ambiguous or unclear. Lastly, FTB asserts that under the rules of regulatory construction, deference should have been given to FTB’s “long-standing interpretation and application of the regulation.”

In our decision, we specifically held that the Regulation was unambiguous, and we declined to follow Example 2 (which expressly states that it is for illustrative purposes) to the extent that it was inconsistent with the unambiguous language of paragraph (2) of subdivision (b) of the Regulation. FTB asserts that Example 2 is part of the Regulation, constitutes FTB’s interpretation, and must be given deference. In *Kisor v. Wilkie* (2019) 139 S.Ct. 2400 [204 L.Ed.2d 841] (*Kisor*), the United States Supreme Court recently examined the rules for the interpretation and construction of an agency’s regulations, particularly the circumstances that warrant deference to an agency’s interpretation of its own regulation. In *Kisor*, the Court clarified the limited scope of the deference doctrine established under *Bowles v. Seminole Rock & Sand Co.* (1945) 325 U.S. 410 and *Auer v. Robbins* (1997) 519 U.S. 452 (*Auer*). The Court explained that “the possibility of deference can arise only if a regulation is genuinely ambiguous.” (*Kisor, supra*, at p. 2414.) Traditional tools of construction must be exhausted before concluding a rule is genuinely ambiguous. (*Ibid.*)

As stated in *Kisor*:

If uncertainty does not exist, there is no plausible reason for deference. The regulation then just means what it means – and the court must give it effect, as the court would any law. Otherwise said, the core theory of *Auer* deference is that sometimes the law runs out, and policy-laden choice is what is left over . . . . But if the law gives an answer — if there is only one reasonable construction of a regulation — then a court has no business deferring to any other reading, no matter how much the agency insists it would make more sense. Deference in that circumstance would ‘permit the agency, under the guise of interpreting a regulation, to create de facto a new regulation.’

(*Kisor*, *supra*, 139 S.Ct. at p. 2415.) We held in our opinion that there is only one reasonable construction of the Regulation: the one based on the clear language of subdivision (b)(2). We find no error in our decision.

With respect to FTB’s assertion that we must find Example 2 to create an ambiguity in the Regulation, it has been stated that “examples set forth in regulations remain persuasive authority *so long as they do not conflict with the regulations themselves*.” (*Cook v. Comm’r* (7th Cir. 2001) 269 F.3d 854, 858; emphasis added.) We agree that conflicts between regulatory language and illustrative examples should be resolved in favor of the regulatory language.

FTB asserts that we should apply what it claims was FTB’s intent and interpretation of the Regulation, rather than the plain language. For that proposition, FTB cites *Dept. of Industrial Relations v. Occupational Safety and Health Appeals Bd.* (2018) 26 Cal.App.5th 93. In that case, the court determined that the word “outdoor” was susceptible to more than one meaning. By contrast, the word “during” in the Regulation is not susceptible to more than one meaning. The word “during” is commonly used to mean “from the beginning to the end of (a particular period)” or “at some time between the beginning and the end of (a period).”<sup>1</sup> Moreover, “[t]he term ‘during’ denotes a temporal link; that is surely the most natural reading of the word as used in the statute.” (*United States v. Ressam* (2008) 553 U.S. 272, 274-275.) It can only mean that an assessment was proposed within one of the four tax years prior to the year for which the current Demand for Tax Return was issued.

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<sup>1</sup> *Cambridge Dictionary Online* <[dictionary.cambridge.org/us/dictionary/English/during](https://dictionary.cambridge.org/us/dictionary/English/during)> [as of September 11, 2019].

A fundamental rule of statutory construction<sup>2</sup> is that we must “examine the actual language of the statute.” (*Draeger v. Reed* (1999) 69 Cal.App.4th 1511, 1520, citing *Halbert’s Lumber Inc. v. Lucky Stores, Inc.* (1992) 6 Cal.App.4th 1233, 1238-1239.) In doing so, we “must accord meaning to every word and phrase in the regulation.” (*Butts v. Bd. of Trustees of Cal. State University* (2014) 225 Cal.App.4th 825, 835.) Only if the plain meaning of a regulation is unclear do we need to proceed to the second step of looking to legislative history. (*Draeger v. Reed, supra.*) Based on the plain meaning of the word “during,” we correctly concluded that FTB failed to apply the demand penalty properly in this case.

FTB asserts that our interpretation of the Regulation would produce absurd results, at least “when compared to the long-standing interpretation of [FTB] and [FTB’s] goal to apply the penalty to repeat nonfilers.” We disagree. Limiting the scope of the demand penalty to those situations authorized by the plain language of the regulation does not produce an absurd result, even if it was not the result that FTB now claims to have intended, which was to give one free pass to taxpayers who failed to file a return. Our interpretation of the Regulation makes sense because the penalty would only be imposed on individuals who had *previously* received notice of the need to comply with the filing requirements by the receipt of the Request or Demand for Tax Return and the Notice of Proposed Assessment during the preceding four taxable years. In fact, if we were to interpret the regulation as FTB proposed it is more likely to produce an absurd result. Because FTB is not precluded from sending a Request or Demand for Tax Return several years after a non-filing, a taxpayer could potentially get the “first” Request or Demand for Tax Return years after the year at issue.<sup>3</sup> Thus, the intended first notice may be issued after the current failure to file, which is exactly what occurred in this case. Appellant did not get notice that he may be subject to a demand penalty until after he had failed to file for the year at issue.

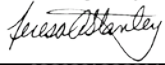
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<sup>2</sup> We note that the rules governing the interpretation of statutes also apply to the interpretation of regulations. (*Diablo Valley College Faculty Senate v. Contra Costa Community College Dist.* (2007) 148 Cal.App.4th 1023, 1037.)

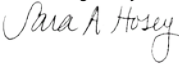
<sup>3</sup> The statute of limitations within which FTB may propose an assessment does not begin to run until a taxpayer files a return. (R&TC, § 19057.) Therefore, FTB may issue a Notice of Proposed Assessment to a non-filer well into the future.

In summary, the application of the Regulation in our decision was not contrary to law and it did not include an error in law. FTB has not demonstrated irregularity in our proceedings; provided newly discovered evidence that could not have been discovered and produced prior to issuance of our opinion; or established that the evidence was insufficient to justify our opinion.

For the reasons set forth above, FTB's petition for rehearing is hereby denied.

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Teresa A. Stanley  
Administrative Law Judge

I concur:

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Sara A. Hosey  
Administrative Law Judge

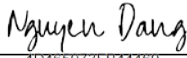
N. DANG, Administrative Law Judge: I respectfully dissent.

The law requires that every word, phrase, sentence and part of a regulation be given significant consideration in discerning its purpose. (*Curle v. Superior Court* (2001) 24 Cal.4th 1057, 1063.) “Interpretations that lead to absurd results or *render words surplusage* are to be avoided.” (*Tuolumne Jobs & Small Business Alliance v. Superior Court* (2014) 59 Cal.4th 1029, 1037, italics added.)

There are no proper grounds for disregarding the illustrative examples contained in California Code of Regulations, title 18, section (Regulation) 19133. These examples were subject to, and approved pursuant to, the rulemaking procedures set forth in California’s Administrative Procedure Act (Register 2004, No. 48), and thus, they are a part of the regulatory language and must be given due consideration.

Further, the majority’s reliance on *Cook v. Comm’r* (7th Cir. 2001) 269 F.3d 854 (*Cook*), is misplaced. *Cook* is merely persuasive authority and should not be relied upon as the sole basis for setting aside well-established principles of statutory construction which require that conflicting language be harmonized to best effectuate the intent and purpose of the drafter. It is also important to note that *Cook* is factually and legally distinguishable from the instant appeal. The court in that case did not address the situation where, as here, an example set forth in the regulation conflicted with other regulatory language, nor does it necessarily follow from the court’s holding that the *only* solution to such a conflict would be to completely disregard the example.

For all the above reasons, as well as those stated in my prior dissenting opinion, I find that the majority opinion is contrary to law, and I would grant the petition for rehearing.

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Nguyen Dang  
Administrative Law Judge

Date Issued: 1/29/2020