



BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
BARBARA P. HUTCHINSON)

Appearances:

For Appellant: Barbara P. Hutchinson,
in pro. per.
For Respondent: Jean Harrison Ograd
Counsel

O P I N I O N

This appeal is made pursuant to section 18593 of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of Barbara P. Hutchinson against proposed assessments of additional personal income tax and penalties as follows:

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	<u>1963</u>	<u>1964</u>	<u>1965</u>
Tax	\$ 777.66	\$ 745.68	\$2,609.83
Penalty - Failure to Furnish Information	194.42	186.42	531.36
Penalty - Delinquent Filing	--	--	121.10
Penalty - Fraud	388.83	372.84	1,304.92
Total Tax and Penalties	<u>\$1,360.91</u>	<u>\$1,304.94</u>	<u>\$4,567.21</u>

The issues for determination are: (1) whether appellant has established any error in respondent's determination of tax and penalties for failure to furnish information and delinquent filing; and (2) whether appellant is liable for civil fraud penalties for the years in issue.

Prior to and during the appeal years appellant was a tax consultant and also prepared tax returns in San Diego. She also owned, in whole or in part, interests in dress shops, a restaurant, a florist shop and a rabbitry. In 1974 respondent learned that appellant had filed a petition with the United States Tax Court contesting federal assessments of tax and civil fraud penalties for the appeal years. Respondent requested that appellant provide information concerning the federal adjustments. When appellant refused to comply, respondent issued deficiency notices reflecting the federal adjustments. Respondent's proposed assessments for all the years also included penalties for delinquent filing and for failure to furnish information after notice and demand, as well as the 50 percent civil fraud penalty. Thereafter, respondent received from the Internal Revenue Service (IRS) a copy of a stipulated judgment of the tax court which had been proposed by appellant. By the terms of the stipulation, appellant agreed to reduced federal deficiencies and fraud penalties for 1963 through 1965. Respondent adjusted its proposed assessments in accordance with the tax court stipulation for the appeal years and notified appellant accordingly. Appellant protested respondent's determination. After a hearing, respondent affirmed its determination of tax and penalties and this appeal followed.

Appellant first contends that respondent is barred by the statute of limitations from assessing additional tax for the appeal years. However, the record on appeal indicates that appellant failed to report to respondent the fact that adjustments were made by the

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IRS to her federal returns for the years in question as required by section 18451 of the Revenue and Taxation Code. Section 18586.2 of the Revenue and Taxation Code provides that where the taxpayer fails to report such federal adjustments as required by section 18451, a notice of proposed deficiency assessment based upon the federal action may be issued by respondent within four years after such action. (Appeal of William G., Jr. and Mary D. Wilt, Cal. St. Bd. of Equal., March 8, 1976; Appeal of Mary R. Encell, Cal. St. Bd. of Equal., April 21, 1959.) Here, appellant was informed of the final federal determination on or about May 28, 1976. Respondent's initial notices of proposed assessment based on federal action were issued November 17, 1975, the prior year. Under the circumstances, appellant's reliance on the statute of limitations is untenable.

Appellant also contends that respondent's proposed assessments for the appeal years were improperly based upon the corresponding federal adjustments for the same years. We have consistently held that a deficiency assessment issued by respondent on the basis of corresponding federal action is presumed to be correct, and that the burden is upon the taxpayer to show that it is incorrect. (Appeal of Paritem and Janie Poonian, Cal. St. Bd. of Equal., Jan. 4, 1972; Appeal of J. Morris and Leila G. Forbes, Cal. St. Bd. of Equal., Aug. 7, 1967.)

Appellant's primary attack on the assessments is based on her assertion that she had no taxable income during the appeal years, and that the amounts which the federal authorities determined were unreported income were actually loans. In fact, the IRS did conclude that substantial amounts of appellant's receipts during the appeal years were loans and not income. This determination is reflected in the IRS agreement to the substantially reduced settlement proposed by appellant. Appellant has produced no evidence to indicate that any additional allowance would be appropriate on this basis.

Appellant also contends that the federal settlement upon which respondent based its action was "coerced." Although appellant has offered no proof of this contention, it is well settled that such a plea has little bearing on the issue of whether the federal action was correct. (Appeal of Ronald J. and Eileen Bachrach, Cal. St. Bd. of Equal., Feb. 6, 1980; Appeal of Donald D. and Virginia C. Smith, Cal. St. Bd. of Equal., Oct. 19, 1973.)

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Since appellant has offered no evidence to indicate that the federal deficiency assessment is incorrect, we must conclude that respondent's action with respect to the deficiency assessments for the appeal years was correct,

It is well settled that respondent's determination of penalties for failure to furnish information upon notice and demand and for delinquent filing are presumptively correct, and the burden is upon the taxpayer to prove them erroneous,, Appeal of Arthur G. Horton, Jr., Cal.. St. Bd. of Equal., Jan. 5, 1982.) Since appellant has offered no evidence to suggest that these penalties were improperly assessed, we must conclude that **respondent's** assessment of these penalties was proper.

With respect to the fraud penalties assessed against appellant, a different question is **presented**. The burden of proving fraud is upon respondent, and it must be established by clear and convincing evidence. (Valetti v. Commissioner, 260 F.2d 185, 188 (3d Cir. 1958); Appeal of-George W. Fairchild, Cal. St. Bd. of Equal., Oct. 27, 1971.) Fraud implies bad faith, intentional wrongdoing, and a sinister-motive; the taxpayer must have the specific intent to evade a tax believed to be owing. (Jones v. Commissioner, 259 F.2d 300, 303 (5th Cir. 1958); Powell v. Granquist, 252 F.2d 56, 60 (9th Cir. 1958).) Although fraud may be established by circumstantial evidence (Powell v. Granquist, supra.), it is never presumed or **imputed**, and it will not be sustained upon circumstances which, at most, create only suspicion. (Jones v. Commissioner, supra, at 303.)

Respondent's position with respect to the propriety of the civil fraud penalties is based on the fact that appellant, a tax **advisor**, proposed and agreed to a federal settlement for the appeal years which included civil fraud penalties. Since the California and federal civil fraud penalties are similar, respondent argues, the fact that appellant proposed and agreed to the **federal** fraud penalty, coupled with the information contained in the federal investigatory report, and **three years** 'of tax deficiencies is sufficient circumstantial evidence to sustain the civil fraud penalties. We cannot agree.

The information contained in the report of the federal investigation and other circumstances **relied** upon by respondent do raise some suspicion 'of fraud.

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Mere suspicion of fraud, however, is insufficient. (Jones v. Commissioner, supra.) The record contains only the conclusionary report of the **federal** investigator and not the various **exhibits**, appendices and affidavits upon which those conclusions were based. In addition, the Supplemental Supporting Statement, which recommended the acceptance of appellant's proposed settlement for an amount substantially less than the IRS's original deficiency assessments, expressed concern with the strength of the federal government's litigating position. The fact that the settlement containing fraud penalties proposed by appellant and accepted by the IRS was substantially less than the IRS's original assessment militates against its use as an admission of fraud by appellant. In any event, we have previously held that respondent may not satisfy its burden of establishing fraud by clear and convincing evidence merely by relying upon a **federal audit** report. (See, e.g., Appeal of William G., Jr., and Mary D. Wilt, Cal. St. Bd. of Equal., March 8 1976.) Accordingly, we cannot conclude that respondent has **established** by clear and convincing evidence that the civil fraud penalty contained in section 18685 of the Revenue and Taxation Code was properly asserted against appellant for any of the appeal years.

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O R 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 18595 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the **protest** of Barbara P. Hutchinson against proposed assessments of additional personal income tax and penalties for failure to furnish information on notice and demand and for delinquent filing in the total amounts of \$972.08, \$932.10 and **\$3,262.29** for the years '1963, 1964 and 1965, respectively, be and the same is hereby sustained, and that the action of the Franchise Tax Board on the protest of Barbara P. Hutchinson against proposed assessments of fraud penalties in the amounts of \$388.83, \$372.84 and **\$1,304.92** for the years 1963, 1964 and 1965, respectively, be and the same is hereby reversed.

Done at Sacramento, California, this 29th day of June , 1982, by the **State** Board of Equalization, with Board **Members** Mr. Bennett, Mr. Dronenburg and Mr. Nevins present.

William M. Bennett , Chairman

Ernest J. Dronenburg, Jr. , Member

Richard Nevins , Member

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