2001-SBE-006-A

BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of	)	
	)	No. 88344
Raymond H. and Margaret R. Berner	)	
	)	

Representing the Parties:

For Appellants: Richard L. Dewberry, Esq.
Joseph A. Vinatieri, Esq.

For Respondent: Natasha Sherwood Page, Tax Counsel

Counsel for Board of Equalization: Donald L. Fillman, Tax Counsel
Craig R. Shaltes, Tax Counsel III

OPINION ON PETITION FOR REHEARING

Background

Upon consideration of the petition for rehearing filed by respondent, we hereby restate and amend our original opinion as indicated below. In its petition, respondent requests the Board to change the wording of our discussion regarding respondent's consideration of declaratory evidence and our discussion about the applicability of the doctrine of collateral estoppel. We believe a change in our original opinion as to the collateral estoppel argument is warranted; in all other aspects, our original opinion remains the same. Therefore, in amending our opinion, we hereby withdraw our previous opinion in this appeal, dated December 20, 2001, and replace it with this opinion; we deny respondent's petition for rehearing, because the arguments set forth in the petition do not constitute sufficient grounds to grant a rehearing. (See *Appeal of Wilson Development, Inc.*, 94-SBE-007, Oct. 5, 1994.)

This appeal is made pursuant to section 19045 of the Revenue and Taxation Code[1] from the action of the Franchise Tax Board on the protest of Raymond H. and Margaret R. Berner against a proposed assessment of additional personal income tax in the following amounts: $95,691.00 tax and a notice and demand penalty of $23,922.75 for 1986; $313,694.00 tax and a notice and demand penalty of $78,423.50 for 1987; and, $49,672.00 tax and a negligence penalty of $3,932.90 for 1988. The primary issue here is whether appellants were residents of California for tax years 1986 through 1988. Respondent argues that this Board's previous decision for tax year 1985 (in which we concluded that appellants were California domiciliaries and residents) is binding on our consideration of the present years. Appellants argue that our 1985 decision was not final because the parties entered into a settlement agreement concerning 1985 (approved by the trial court, but agreed by the parties to not affect subsequent tax years).

Facts and Contentions

Appellants were long-term domiciliaries and residents of California prior to their marriage in 1980. At that time they moved into a 4,637 square foot home in Solana Beach, California (San Diego County) which appellant-husband had purchased in 1977. In December 1980, they purchased a 1,550 square foot home in Stateline, Nevada. Also in 1980, appellant-husband inherited his mother's 1,808 square foot San Diego condominium. These were the three residences owned through 1985 that were the basis of this Board's prior decision—for years 1981 through 1985. For those prior years, the Board concluded that appellants had failed to carry their burden of proof that their domicile had changed from California to Nevada. The present appeal raises the same issues of residency and domicile that were before the Board for 1981 through 1985. However, since the Board's prior decision found that appellants had not established a change in domicile for 1981 through 1985, the further issue raised is whether the Board's prior decision binds it in any way for the present years.

Respondent argues that the Board's prior decision—that appellants were domiciliaries and residents of California for 1985—is the necessary starting point for the present appeal. It argues that the issue of domicile for 1985 was previously litigated and decided by the Board—therefore, the doctrine of collateral estoppel forbids the issue to be relitigated for years 1981 through 1985. Respondent argues, in effect, that this Board must base the present opinion upon the fact that appellants were domiciliaries of California on December 31, 1985. This would require appellants to carry the burden of proving that their domicile changed from California to Nevada on or after January 1, 1986—

[1] Unless otherwise specified, all section references are to sections of the Revenue and Taxation Code in effect for the years in issue.

and the only facts that the Board should consider are those occurring after 1985. For reasons discussed later in this opinion, the Board rejects this premise.

The following transactions occurred during the years presently in issue with respect to appellants' residences: (1) in November 1986, appellants purchased a 2,684 square foot home in Glenbrook, Nevada (near Stateline, Nevada); (2) in September 1988, appellants purchased a 2,773 square foot home in Indian Wells, California; and (3) in November 1988, appellants sold their 4,637 square foot home in Solana Beach, California.

Respondent examined the present three years (1986 through 1988) as a result of its former audit. When no returns were filed, respondent contacted appellants. Appellants then filed a California Nonresident Personal Income Tax Return for 1988 only. This was the year appellants sold the Solana Beach home for $750,000, with resultant California-source income. Respondent issued Notices of Proposed Assessment (NPA) for each year based on appellants' federal returns. From the information it gathered, respondent concluded that appellants had the closest connection, during 1986 through 1988, with California. It further concluded that appellants did not show evidence of a change of domicile from California to Nevada during the three years in issue. Thus, respondent contends that appellants never permanently left California.

Respondent noted that appellants had a membership in a country club near their home in Solana Beach, California, which was used extensively until September 1988, when they purchased their home in Indian Wells, California. Appellants then joined a country club in Indian Wells, California, in November 1988. Respondent contends that appellants' utility bills from California were larger than those from Nevada for all three years. Respondent used cancelled checks that it obtained from the Bank of America in Nevada to conclude that more of the type of contacts that correspond with a residence occurred in California than Nevada for the years in issue. Included were purchases of goods and services, including contacts with medical and dental offices and weekly maintenance of the California home (housekeeper, gardener, pool service, and security). Respondent also attempted to reconstruct the number of days that appellant spent each year in California and Nevada (appellants also traveled to other states and countries during this period). Of the days for which respondent believes it could account, it concluded that appellants spent more days in California than Nevada in 1986 and 1988, and more days in Nevada than California in 1987. Respondent also concluded that appellants made more bank deposits in California than Nevada in each year, and had more credit card transactions in California in 1986 and 1988, but more in Nevada for 1987. Respondent also noted that appellants had retained a California attorney to represent them in the dispute with respondent.

Appellants contend that they spent approximately four months each year in California, seven months in Nevada, and one month elsewhere. They contend that the time spent in California was primarily during the winter months when there was snow at their home in Nevada, although appellants acknowledge that they spent most of the Christmas holidays in Nevada. Appellants dispute

respondent's conclusions concerning days spent in California and Nevada, as well as respondent's conclusions from the credit card usage and bank transactions. They indicate that some of the credit card transactions attributed by respondent to California were actually transactions that occurred when they crossed the border near Stateline or when a business near Stateline used a California bank. Appellants provided documentary evidence to support this contention. They also provided evidence that extensive catalog purchases were made while residing in Nevada from California based mail order vendors that respondent contended were California credit card transactions.

Appellants contend that appellant-husband's frequent golf games were much more frequent in Nevada than California—but there were no country clubs to join (during those years) near their Nevada residence. Thus, nearby public courses (without the same record keeping) were the ones used while living in Nevada. With their supplemental brief dated February 9, 2001, appellants provided over 30 affidavits and declarations from friends, relatives, and professional individuals concerning appellants' contacts with Nevada. Golfing friends stated that they had played golf with appellant-husband in Nevada throughout the year, or in California during the period of January through April, or visited appellants in their Nevada home at various times of the year. Several affidavits support appellants' contention that more time was spent in Nevada than in California during the years in issue. Several indicate that the signatory kept in contact with appellants frequently by telephone at the Nevada residence—not the California residence. Several indicate that appellants' lives were centered in Nevada. One affidavit is from the Postmaster of Glenbrook, Nevada, indicating that he had became familiar with appellants when they came to pick up their mail, at least weekly; and, when appellants were on vacation they would provide directions for handling their mail.

Appellants also noted that during the years in issue they: each had a Nevada driver's license; were registered to vote in Nevada; used a Nevada bank; registered most of their automobiles in Nevada; and, maintained their permanent home and abode in Nevada. They contend that their retention of a residence in California, and their use of that residence, was consistent with that of a seasonal visitor to California. Appellants did not claim a homeowners' tax exemption on any of the California property.

Applicable Law

Burden of Proof and Presumptions on Appeal. Respondent's determination of an assessment is presumed correct and appellant has the burden of proving it to be wrong. (*Todd v. McColgan* (1949) 89 Cal.App.2d 509; *Appeal of Myron E. and Alice Z. Gire*, 69-SBE-029, Sept. 10, 1969; *Appeal of Ismael R. Manriquez*, 79-SBE-077, Apr. 10, 1979.[2]) Respondent's determination of residency is also presumptively correct. (*Appeals of John R. Young*, 86-SBE-199, Nov. 19, 1986.) The burden of proof as to a change of domicile is on the party asserting such change.

[2] State Board of Equalization ("SBE") opinions can be viewed on our website (www.boe.ca.gov).

(*Sheehan v. Scott* (1905) 145 Cal. 684, revd. on other grounds in *Zeilanga v. Nelson* (1971) 4 Cal.3d 716; *Appeal of Terance and Brenda Harrison*, 85-SBE-059, June 25, 1985.) If there is doubt on the question of domicile after the facts and circumstances have been presented, the domicile must be found to have not changed. (*Whitmore v. Commissioner* (1955) 25 T.C. 293; *Appeal of Anthony J. and Ann S. D'Eustachio*, 85-SBE-040, May 8, 1985.) Respondent's imposition of most penalties, including those in issue, is also presumed correct (see, e.g., *Appeal of W. L. Bryant*, 83-SBE-180, Aug. 17, 1983; *Appeal of Robert Scott*, 83-SBE-094, Apr. 5, 1983; and *Appeal of Thomas T. Crittenden*, 74-SBE-043, Oct. 7, 1974).

Domicile and Residency. Section 17041 imposes a tax on every "resident" of California. Section 17014, subdivision (a), assigns resident status to "[e]very individual who is in this state for other than a temporary or transitory purpose." Subdivision (b) deals with California domiciliaries who are absent from the state, and provides that every such individual "who is outside the state for a temporary or transitory purpose" is a resident. The key question under either subdivision is whether the taxpayer's purpose in entering or leaving California was temporary or transitory in character. This determination cannot be based on the taxpayer's subjective intent, but must instead be based on objective facts. (*Appeals of Nathan H. and Julia M. Juran*, 68-SBE-004, Jan. 8, 1968.)

Proof of Non-Residence. California Code of Regulations, title 18 (Regulation), section 17014, subdivision (d), states that the type and amount of proof cannot be specified by general regulation. However, ordinarily affidavits or testimony of an individual and of his friends, employer, or business associates that the individual was in California for rest or vacation will be sufficient to overcome any presumption of residency in California. Regulation section 17014, subdivision (b), provides that an individual whose presence in California does not exceed an aggregate of six months within the taxable year, and who is domiciled without the state and maintains a permanent abode at the place of his domicile, will be considered as being in this state for temporary or transitory purposes provided he does not engage in any activity or conduct in the state other than that of a seasonal visitor, tourist or guest.

Whether a taxpayer's purpose in entering or leaving California is temporary or transitory in character is essentially a question of fact to be determined by examining all the circumstances of each particular case. (See *Appeal of Michael T. and Patricia C. Gabrik*, 86-SBE-014, Feb. 4, 1986.) In situations where the taxpayers have significant contacts with more than one state, as appellants do here, the state with the closest connections during the taxable year is the state of residence. (Cal. Code Regs., tit. 18, § 17014, subd. (b).) Consistent with this regulation, the Board has held that the contacts which taxpayers maintain in this and other states are important objective indications of whether their presence in, or absence from, California was for a temporary or transitory purpose. (*Appeal of Richards L. and Kathleen K. Hardman*, 75-SBE-052, Aug. 19, 1975; *Appeal of Anthony V. and Beverly Zupanovich*, 76-SBE-002, Jan. 6, 1976.) Such contacts are important as a measure of the benefits and protection that the taxpayers have received from the laws and government of California and

as objective indicia of whether the taxpayers entered or left this state for temporary or transitory purposes. (*Appeal of Anthony V. and Beverly Zupanovich*, *supra*.)

"Domicile" refers to the place where individuals have their true, fixed, permanent home and principal establishment, and to which place they have, whenever they are absent, the intention of returning. "It is the place in which a [person] has voluntarily fixed the habitation of [themselves] and [their] family, not for a mere special or limited purpose, but with the present intention of making a permanent home." (Cal. Code Regs., tit. 18, § 17014, subd. (c).) In order to change one's domicile, one must actually move to a new residence and intend to remain there permanently or indefinitely. (*In re Marriage of Leff* (1972) 25 Cal.App.3d 630, 642.) A person may have only one domicile at a time. (Cal. Code Regs., tit. 18, § 17014, subd. (c).) One's acts must give clear proof of a current intention to abandon the old domicile and establish a new one. (*Chapman v. Superior Court* (1958) 162 Cal.App.2d 421.) However, a person whose domicile is in another state or country will be taxed in California if he or she is found to be a "resident" of California. Similarly, a person who is domiciled in California may escape California tax if he or she is not a "resident" of California.

Thus, if it is determined that appellants were Nevada domiciliaries, it must also be determined whether their presence in California was for a temporary or transitory purpose. And, if it is determined that appellants were California domiciliaries, it must also be determined whether their presence in Nevada was for a temporary or transitory purpose. (See discussion, *supra*, regarding whether a taxpayer's purpose for entering or leaving California is temporary or transitory in character.)

Res Judicata (Including Collateral Estoppel). The doctrine of res judicata gives conclusive effect to a prior judgment or decision. It has two aspects: (1) the prior judgment is a complete bar to a subsequent action so far as the subsequent action is on the same cause of action; and (2) the prior judgment is conclusive as to issues actually litigated between the parties in the former action if the subsequent action is on a different cause of action. Thus, under the second aspect, "collateral estoppel" (issue preclusion)[3] forbids a party from relitigating the same issues even if the cause of action is different. (See 7 Witkin, *supra*, §281, p. 821; *Bernhard v. Bank of America* (1942) 19 Cal.2d 807; *Appeal of Eli A. and Virginia W. Allec*, 75-SBE-004, Jan. 7, 1975.) Collateral estoppel has been applied in tax cases. (*Calhoun v. Franchise Tax Board* (1978) 20 Cal.3d 881.)

The Second Restatement of Judgments, section 13, provides as follows:

[3] The term "collateral estoppel" was used in the first Restatement of Judgments, and is now in common use. The Second Restatement of Judgments uses the term "issue preclusion." (7 Witkin, Cal. Procedure (4th ed. 1997) Judgment, §354, p. 915.)

> "However, for purposes of issue preclusion (as distinguished from merger and bar), 'final judgment' includes any prior adjudication of an issue in another action that is determined to be *sufficiently firm* to be accorded conclusive effect."

(Emphasis added.) This concept was applied in *Sandoval v. Superior Court* (1983), 40 Cal.App.3d 932, 937, where the court applied collateral estoppel to a trial court judgment—even though the parties reached a post-decision settlement. The court stated: "the Restatement analysis and reason itself dictate that the trial court judgment reemerges with sufficient finality to permit the application of collateral estoppel." (*Id.*) Thus, we conclude that the Board's decision for the prior years (1981—1985) was a final decision, notwithstanding the fact that the parties reached a subsequent settlement.

However, we note that the doctrine of collateral estoppel is "not an inflexible, universally applicable principle; policy considerations may limit its use where the limitation on relitigation underpinnings of the doctrine are outweighed by other factors." (*Jackson v. City of Sacramento* (1991) 117 Cal.App.3d 596, 603.) In the present appeal, appellants have presented substantially more evidence in support of their position than they did in their previous appeal. Therefore, we choose not to apply collateral estoppel to this appeal.

Penalties. Former section 18683 (renumbered to § 19133, operative Jan. 1, 1994) provides that, if a taxpayer fails to file a return upon notice and demand by respondent, the taxpayer will incur a penalty unless the taxpayer can establish that "the failure is due to reasonable cause and not willful neglect." The penalty is computed as 25 percent of the total tax, determined without regard to payments or other credits. (*Appeal of Robert Scott*, *supra*.) To establish reasonable cause, a taxpayer must demonstrate that he or she exercised ordinary business care and prudence. (*Appeal of Stephen C. Bieneman*, 82-SBE-148, July 26, 1982.) In order to overcome the presumption of correctness of a penalty, the taxpayer must provide credible and competent evidence to support the claim of reasonable cause; otherwise, the penalty will not be abated. (*Appeal of Winston R. Schwyhart*, 75-SBE-035, Apr. 22, 1975.)

Former section 18684 provided for a "negligence" penalty of five percent of the total amount of the applicable deficiency.[4] Negligence includes any failure to make a reasonable attempt to comply with the provisions of the Internal Revenue Code. In the present appeal, appellants failed to file a timely California Personal Income Tax return for 1988 even though they sold the Solana Beach, California, residence (acquired in 1977) for $750,000. Respondent imposed the penalty for negligence only for tax year 1988. We held in *Appeal of Greg L. Dexter*, decided on May 6, 1986, as follows:

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[4] Former section 18684 was repealed effective July 31, 1990. It was replaced by section 19164 (which incorporates the provisions of Internal Revenue Code section 6662) and provides for an "accuracy-related" penalty, including a penalty for negligence, of 20 percent of the applicable underpayment.

> "[A] deficiency is the difference between the taxpayer's correct tax liability and the amount of tax shown on his original return. In the case where a delinquent return is filed, the tax shown on such return does not reduce the amount of the deficiency. [Citations omitted.] Since appellant did not file a timely return, a deficiency existed in the amount of his total tax liability, and the negligence penalty was properly computed on that amount."

Thus, an underpayment is not reduced by the amount of tax liability shown on a return that is not timely filed.

Conclusions

We conclude that appellants have established through affidavits and declarations of friends, family, and professionals (sufficient proof under Regulation section 17014, subdivision (d)) that they changed their domicile from California to Nevada, effective for each of the three tax years in issue, and their primary residence for each of these years was in Nevada. We find from the declarations that appellants' presence in California did not exceed six months in any taxable year and that their activity in this state was that of a seasonal visitor. The fact that the appellants owned a home in California and belonged to a California golf club does not change these findings. The fact that appellants utilized the services of a California attorney should have no effect on the determinations. We also conclude that appellants have established reasonable cause for failing to file California personal income tax returns for the two tax years in which they did not have California-source income (1986 and 1987). Therefore, the proposed tax on non-California-source income is reversed and the notice and demand penalties imposed for 1986 and 1987 will be abated. For 1988 (the year which appellants eventually filed a late return showing California-source income), we conclude that the portion of the negligence penalty applicable to the California-source income was proper; the remaining portion of this penalty will be abated.

We also find that respondent should ordinarily follow the evidence guideline of Regulation section 17014, subdivision (d), which it adopted pursuant to Revenue and Taxation Code (former) section 9253, and current section 19503. In this case, respondent failed to reasonably consider the declarations and evidence provided by appellants.

We deny respondent's petition for rehearing, and restate and amend our original decision as indicated above.

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 19047 of the Revenue and Taxation Code, that the petition for rehearing filed by respondent is denied and that our original opinion in this matter is restated and amended as reflected in the attached written opinion. The action of the Franchise Tax Board on the protest of Raymond H. and Margaret R. Berner against a proposed assessment of additional personal income tax in the amounts of $95,691.00 and penalty of $23,922.75 for 1986, $313,694.00 and penalty of $78,423.50 for 1987, be and the same are hereby reversed. The action of the Franchise Tax Board on the protest against a proposed assessment of additional personal income tax in the amount of $49,672.00 and penalty of $3,932.90 for tax year 1988, be and the same are hereby modified to include only the tax and penalty applicable to California-source income.

Done at Sacramento, California, this 1st day of August, 2002, by the State Board of Equalization, with Board Members Mr. Chiang, Mr. Klehs, Mr. Parrish, and Ms. Marcy Jo Mandel present.

Mr. John Chiang, Chairman

Mr. Johan Klehs, Member

Mr. Claude Parrish, Member

*Ms. Marcy Jo Mandel, Member

_____, Member

*For Kathleen Connell per Government code section 7.9.

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