94-SBE-013

BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of	)	
	)	No. 93A-0498
CLIFFORD L. AND LINDA SCHAFFER	)	
	)	

Appearances:

For Appellant:	Kevin C. Kellow Attorney At Law
For Respondent:	John Penfield Counsel

O P I N I O N

This appeal is made pursuant to section 19045[1/] of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of Clifford L. and Linda Schaffer against a proposed assessment of additional personal income tax in the amount of $1,973 for the year 1982.

The Internal Revenue Service (IRS) audited appellants' 1982 tax year, disallowed appellants' partnership losses attributable to Harvest Research, and issued a deficiency notice. Appellants responded by filing a petition in the U.S. Tax Court, which assigned it docket number 25499-87. The parties entered into a closing agreement which the appellants signed on January 7,

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[1/] Unless otherwise specified, all section references hereinafter in the text of this opinion are to sections of the Revenue and Taxation Code as in effect for the year in issue.

1988. The closing agreement was forwarded to IRS District Counsel, who signed it on February 1, 1988. A stipulated U.S. Tax Court judgment, based on the closing agreement, was filed on March 2, 1988. Appellants did not advise respondent of the closing agreement or stipulated judgment. Respondent issued a notice of proposed assessment (NPA) on March 3, 1992. Appellants contested the NPA, stating that it was issued beyond the statute of limitations applicable to deficiencies arising out of federal adjustments. Respondent affirmed its action on January 4, 1993, and this timely appeal followed.

Appellants contend that the statute of limitations commenced to run on February 1, 1988, the date when the closing agreement was signed both by appellants and the IRS. Respondent argues the statute of limitations commenced to run on the date when the stipulated Tax Court judgment became final. Under I.R.C. section 7481(a), the stipulated judgment became final on May 31, 1988, the 90th day after it was filed in the Tax Court. The issue presented turns on the meaning and application of the statute of limitations set forth in Revenue and Taxation Code section 18586.2:

> If a taxpayer fails to report a change or correction by the Commissioner of Internal Revenue or other officer of the United States or other competent authority or fails to file an amended return as required by Section 18451, a notice of proposed deficiency assessment resulting from the adjustment may be mailed to the taxpayer within four years after the change, correction, or amended return is reported to or filed with the federal government.

The California Supreme Court has stated that "in construing statutes levying taxes, [we] may not extend their provisions by implication beyond the clear import of the language used, nor enlarge upon their operation so as to embrace matters not specifically included." <u>Edison California Stores, Inc.</u> v. <u>McColgan</u>, 30 Cal.2d 472, 477 (1947). Our function is to ascertain what is in terms or in substance contained in the statute, not to insert what has been omitted or to omit what has been inserted.

Respondent urges us to follow a series of federal decisions including <u>Pesko</u> v. <u>United States</u>, 918 F.2d 1581 (Fed. Cir. 1990), <u>Sherry Frontenac, Inc.</u> v. <u>United States</u>, 868 F.2d 420 (11th Cir. 1989), and <u>Security Industrial Insurance Co.</u> v. <u>United States</u>, 830 F.2d 581 (5th Cir. 1987). These cases held that the three year statute of limitations contained in I.R.C. sections 6501 and 6503(a) does not commence to run until 90 days after stipulated judgments are filed with the Tax Court. The results reached in these cases, however, are explained by the particular wording of I.R.C. section 6503(a)(1) which states, in relevant part: "The running of the period of limitations provided in section 6501...shall...be suspended...if a proceeding in respect of the deficiency is placed on the docket of the Tax Court, <u>until the decision of the Tax Court becomes final</u>...." The wording of Revenue and Taxation Code section 18586.2 is considerably different. Instead of focusing on the date when a decision of the Tax Court becomes <u>final</u>, the statute instead focuses on when a change or correction is <u>filed</u> with the federal government. In view of the significant differences between the language of Revenue and Taxation Code section 18586.2 and I.R.C. section 6503(a)(1), we do not believe that the federal decisions cited by respondent are entitled to deference. Rather, a straight forward interpretation of the language of Revenue and Taxation Code section 18586.2 would indicate that where a Tax Court proceeding is resolved by a stipulated judgment, the date the judgment is entered by the Tax Court rather than the date it becomes final triggers the running of the statute.

In support of its contention that its proposed assessment is not barred, respondent has cited to Cal. Code Regs., tit. 18, section 18586.3(e), which concerns the period of limitation for proposing a deficiency after federal changes. This regulation states: "A final determination is an irrevocable determination or adjustment of a taxpayer's federal tax liability from which there exists no further right of appeal either administrative or judicial." Assuming this regulation comports with the purpose and intent of the Legislature, we do not see that it supports respondent. The regulation defines finality in terms of whether there is a further "right of appeal," administratively or judicially. In the specific context of stipulated judgments made in the Tax Court, it has been held the taxpayer impliedly "waives his or her right to appeal" from the stipulated judgment. White v. Commissioner of Internal Revenue, 776 F.2d 976, 977 (11th Cir. 1985).[2/] Thus, the regulation read together with White supports the taxpayer in this case.

Respondent further directs our attention to Example 2 set forth in the foregoing regulation. It provides: "The 90-day deficiency notice pursuant to Section 6213(a) of the Internal Revenue Code of 1986 is a final determination, unless a timely petition to redetermine the deficiency is filed in the Tax Court of the United States, in which event the judgment of the court of last resort affirming the deficiency, or the redetermination of the deficiency pursuant to a judgment of the court of last resort is the final determination. But the determination does not become final until the time for petitioning for a rehearing or appealing to a higher court has expired." Again, assuming this regulation fairly interprets the statute, we do not find it to be persuasive. Nothing in the example suggests it is to have any application where the deficiency is determined by a stipulation of the parties. In our view, the foregoing example applies only where the deficiency is determined by a judgment of the court following an adversarial hearing where there has been no implied or express waiver of the right to appeal.

Any other interpretation would disregard the wording of Revenue and Taxation Code section 18586.2. Clearly, the statute does not refer to when the time for appealing to a higher court has expired. Rather, the statute is phrased in terms of when the change in federal liability is filed with the government. Further, in examining this statute, we must remain mindful of the decision in Dryer's Grand Ice Cream, Inc. v. County of Alameda, 178 Cal.App.3d 1174 (1986). The issue presented in that decision was when the statute of limitations contained in Revenue and Taxation Code section 532 commences to run. In affirming a judgment for the taxpayer, the Court of Appeal stated it is "well settled that in case of doubt statutes levying taxes are construed most strongly against the government and in favor of the taxpayer." Id. at 1182.[3/]

[2/] White indicated there are two exceptions to the rule that there is no right to appeal a stipulated judgment. The exceptions are where a party to the stipulation did not actually consent or where the court lacks subject matter jurisdiction to enter the judgment. If the record in this case demonstrated the IRS or the taxpayers had appealed on either of these grounds, an entirely different situation would be presented in this matter.

[3/] This rule of construction further distinguishes this case from the holding in Sherry Frontenac, Inc. v. United States, supra. In ruling for the IRS in that case, the court relied on a U.S. Supreme Court decision which held statutes of limitation barring the collection of federal taxes must be strictly construed in favor of the government. Id. at 423. Of course, our mandate is to follow Dryer and a prior California Supreme Court case, Edison California Stores v. McColgan, 30 Cal.2d 472, 476 (1947), directing us to construe statutes barring the collection of state taxes in favor of the taxpayer.

In conclusion, because respondent in this case issued its proposed assessment more than four years after the stipulated judgment was entered by the Tax Court, we conclude that the proposed assessment is barred by Revenue and Taxation Code section 18586.2. Accordingly, respondent's action here must be reversed.

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 action of the Franchise Tax Board on the protest of Clifford L. and Linda Schaffer against a proposed assessment of additional personal income tax in the amount of $1,973 for the year 1982 be and the same is hereby reversed.

Done at Culver City, California, this 14th day of December, 1994 by the State Board of Equalization, with Board Members Mr. Sherman, Mr. Dronenburg and Ms. Scott* present.

Brad Sherman, Chairman

Ernest J. Dronenburg, Jr., Member

________________, Member

________________, Member

*For Gray Davis, per Government Code section 7.9.