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3/20/2023

Via E-Mail [regulations@ota.ca.gov]

RE: COMMENTS IN RESPONSE TO PROPOSED AMENDMENTS TO OTA RULES FOR TAX APPEALS.

The proposed revisions to the OTA's regulation Section 30104 attempt to limit the OTA's jurisdiction in a manner that is inconsistent with the OTA's jurisdictional powers. Specifically, the proposed language in Subsection (d), (d)(1), and (d)(2), provides that the OTA does not have jurisdiction to decide the question of whether a provision in the California Code of Regulations is invalid or unenforceable on the basis that it conflicts with another regulation or with a provision of the Revenue and Taxation Code. As explained below, the OTA does have jurisdiction over such matters, and to limit the OTA's jurisdiction will also create unnecessary and burdensome financial and procedural barriers to taxpayers seeking to resolve their California tax matters.

1. OTA HAS THE POWER TO HEAR ALL MATTERS RELATED TO THE CORRECT AMOUNT OWED OR DUE BY A TAXPAYER.

The OTA's powers are derived from its enabling legislation, Assembly Bill Numbers 102 and 131, which "transfer[red] to the office [of Tax Appeals] the various duties, *powers*, and responsibilities of the State Board of Equalization necessary or appropriate to conduct appeals hearing".[1] Thus, not surprisingly, OTA Regulation Section 30104, which defines the OTA's jurisdiction, is similar to the CCR section 5412, the regulation that, before its repeal, defined the jurisdiction of the Board of Equalization's ("BOE"). It is important to know the chronological history of the BOE's regulatory language and subsequent case law to understand why the

[1] Assembly Bill Nos. 102 and 131 (2017-2018 Reg. Sess.).

proposed revision to the OTA's regulation is inconsistent with the OTA's legislatively granted authority.

CCR section 5412 provided the BOE with the authority to "hear and decide a timely filed appeal" as long as certain procedural requirements were met.[2] The Regulation went on to state that the BOE's "jurisdiction is limited to determining the correct amount owed by, or due to, the appellant [(e.g., FTB)] for the year or years at issue in the appeal."[3] The Regulation further specified issues that the BOE did not have the jurisdiction to hear.[4] Relevant here is that the BOE did not have the jurisdiction to determine "[w]hether a California statute or regulation is invalid or enforceable *under the Federal or California Constitutions*, unless a federal or California appellate court has already made such a determination."[5]

Thus, under historical CCR section 5412(b), the BOE had jurisdiction to consider all issues related to "determining the correct amount owed by…the appellant [(e.g., FTB)]" *except* if the issue deals with invalidating a statute or regulation under the "*Federal or California Constitutions*."[6] Under the framework of CCR section 5412, the BOE held in *Appeal of Save Mart* that CCR section 23643-3 was invalid because it "alters and enlarges on the words of the statute."[7] Of course, the BOE could not invalidate CCR section 23643-3 on constitutional grounds due to the jurisdictional limitations set forth in CCR section 5412. But it could do so on statutory grounds.

Therefore, the BOE was given broad powers to hear all issues dealing with whether amounts were owed by or due to the FTB. That power was limited in the regulations which prevented the BOE from invalidating statutes or regulations on *constitutional* grounds. This was affirmed by the BOE's decision in *Appeal of Save Mart.*

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2 *See* CCR § 5412(a)(1)-(10). For example, FTB must mail a Notice of Action or 6 months must pass before a deemed denial.

3 CCR § 5412(b).

4 CCR § 5412(b)(1)-(5).

5 CCR § 5412(b)(1) (emphasis added).

6 *Id.*

7 2002 Cal. Tax LEXIS 80, page 9.

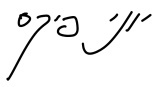
Given that the legislature granted, and transferred to, the OTA the "duties, powers, and responsibilities" previously granted to BOE, it appears logical that the OTA is well within its jurisdictional rights to entertain matters involving validity and enforceability of regulations that conflict with provisions of the Revenue and Taxation Code (i.e., no constitutional challenge involved), and conflicts with other regulations (i.e., no constitutional challenge involved), before a federal or California appellate court has made a determination on that issue.

2. **LIMITING THE OTA'S JURISDICTION WILL CREATE UNNECESSARY FINANCIAL AND PROCEDURAL BARRIERS AND BURDENS FOR TAXPAYERS SEEKING TO RESOLVE THEIR TAX DISPUTES.**

Lastly, adding such language to limit the OTA's jurisdiction will have the significant negative impact of imposing unnecessary financial and administrative barriers and burdens on taxpayers seeking to resolve their tax disputes. These proposed changes would require taxpayers to pay disputed tax assessments (i.e., "pay to play") and incur additional litigation costs in order to pursue such matters at court, despite the fact that the OTA is well within its powers to decide such matters and its administrative law judges are well equipped to rule on such tax questions.

The proposed changes to the Section 30104 would go against the legislative intent behind the Taxpayer Transparency and Fairness Act of 2017, where the legislature declared that "California taxpayers are entitled to a tax administration and appeals process that is fair, transparent, consistent, equitable, and impartial…[and] [o]ne of the most fundamental aspects of a good tax system is a fair and *efficient* appeals process." (Emphasis added). These proposed changes to Section 30104 would thwart the legislature intent behind establishing the OTA.

Regards



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March 20, 2023

BY EMAIL TO REGULATIONS@OTA.CA.GOV
Office of Tax Appeals
P.O. Box 989880
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Re: Proposed Amendments to OTA Rules for Tax Appeals (2023, No. 1)
Interested Parties Meeting: March 20, 2023

Dear Sir or Madam:

This letter contains my initial comments on your proposed amendments to the Rules for Tax Appeals, that were released in conjunction with the Notice of Interested Parties ("IP") Meeting for March 20, 2023. I have over 40 years of experience in tax controversy and litigation matters, including all manner of local, state and federal tax disputes, in private practice and in public service. I had been expecting to attend and participate in the IP meeting. However, a conflict has arisen in my schedule and it is uncertain whether the short period that I may be able to attend the IP meeting will accommodate the making of these initial comments. I am making these comments on my own behalf in the interest of fair tax administration. Although I represent appellants before the Office of Tax Appeals ("OTA"), my work on these comments was not requested by any client.

Your Notice indicates that the proposed amendments are meant to reflect recent statutory changes made by Senate Bill 189, Stats. 2022, Ch. 48, and that you are also proposing "miscellaneous comprehensive cleanup amendments." The former is standard for regulatory amendments that actually reflect particular statutory changes. The latter might be appropriate for clarifying amendments to existing regulations but is not appropriate for staking out new substantive changes.

1. Section 30101.5 (Inapplicability of Division 2.1): This proposed amendment, an entirely new regulation, states that, as of the January 1, 2018 start date for certain tax appeals to be handled by OTA, that the State Board of Equalization's ("BOE's") Rules for Tax Appeals no longer apply, but that OTA's own Rules for Tax Appeals apply instead. While Gov. Code § 15679 required OTA to adopt regulations by January 1, 2018, I note that, according to the OTA website, OTA itself had no Rules for Tax Appeals in place (effective) until January 5, 2018. January 2-4, 2018 were business days. While it is unknown whether there may be any adverse impacts on appeals as a result of the proposed amendment's attempt to backdate the operative or effective date of OTA's Emergency Regulations, the attempt does seem improper. In addition, OTA is currently on its third version of the OTA Rules for Tax Appeals. The addition of the proposed amendment raises a question as to whether OTA is attempting to state a January 1, 2018 operative and effective date for all of its proposed amendments now and in the future. While I suspect such may not be your intent, any such attempt or interpretation is objectionable. I

suggest you make clear that any amendments to the Rules for Tax Appeals are operative and effective only as of their respective effective date(s) under the Administrative Procedure Act following approval by the Office of Administrative Law.

2. Section 30102 (Definitions): You have deleted the definition of "FTB," and Franchise Tax Board is not short-titled elsewhere in the Rules for Tax Appeals or the proposed amendments. The definition should be reinstated.

3. Section 30102 (Definitions): You have deleted the longstanding standard for admissibility of evidence ("the sort of evidence responsible persons are accustomed to rely on in the conduct of serious affairs") that currently appears in your definition of "written record." As no explanation accompanied any of the proposed amendments, it is unknown why this proposed amendment is being proffered, but the deletion might be viewed as a substantive change of long-standing administrative practice and could be detrimental to taxpayers, particularly to the large cohort of small businesses and individuals who bring their appeals before OTA. I suggest reinstating the statement proposed to be deleted. It is possible your proposed deletion of (8) in the definition of "written record" was an editing choice on grounds that the proposed additional language in (5) is inclusive of all evidence not objected to and all evidence the Panel includes over an objection. If that was your thinking, I suggest you find a place in your proposed amendments to retain the long-standing admissibility standard. "Miscellaneous comprehensive cleanup amendments" should not work, or potentially work, a substantive change in taxpayer's rights.

4. Section 30104 (Limitations on Jurisdiction): The proposed amendment to subsection (a), whereby OTA proposes to expand upon Article III, section 3.5, of the California Constitution, which is currently reflected in this section, and decline jurisdiction to "otherwise refuse to follow an applicable statutory provision" is curious. Certainly, OTA must apply applicable statutes using the normal rules of statutory construction and must seek to harmonize statutes when they appear to be in conflict. The proposed amendment is curious because it is unknown what OTA is seeking to avoid doing. Is OTA seeking to be held to some but not all the rules of statutory construction? Is OTA inartfully stating what it thinks the result would be in a particular case or cases, perhaps even in a case or cases that are pending, if a taxpayer's view of how to harmonize or interpret the statutes at issue were to prevail? Does OTA think that applying standard rules of statutory construction might result in OTA not "following" an applicable statute? The proposed amendment to (a) should be deleted.

5. Section 30104 (Limitations on Jurisdiction): The proposed amendment adding new subsection (d), whereby OTA proposes to repurpose the language of Article III, section 3.5, of the California Constitution in order to disavow any power to find a regulation invalid or unenforceable should be deleted. Nothing in the recent legislation authorizes this proposed amendment and the proposed amendment falls outside the parameters of what could fairly be considered miscellaneous cleanup. Your addition of *Newco Leasing, Inc. v. State Board of Equalization* to the reference authorities for Section 30104 at most *might* support stating, as you propose in (d)(3) that "OTA does not have jurisdiction to determine whether a provision of OTA's Rules for Tax Appeals is invalid or to refuse to follow the regulation on that basis."

Article III, section 3.5, of the California Constitution was adopted by the voters on June 6, 1978 when they passed Proposition 5, which had been placed on the ballot by the Legislature. The California Public Utilities Commission ("CPUC") had declared a statute invalid, reasoning that it was unconstitutionally vague. The California Supreme Court found "nothing vague or unintelligible" in the statute and annulled the CPUC decision, while stating that the CPUC could determine the validity of statutes. *Southern Pacific Transportation Company v. Public Utilities Commission* (1976) 18 Cal.3d 308, at 311 and fn.2, 314-315. The Legislature put Proposition 5 on the ballot to make clear that an administrative agency, even one granted broad quasi-judicial powers by the Constitution or by the Legislature itself, could not override the will of the people as expressed through their legislators. *Proposition 5 (Administrative Agencies), California Voters Pamphlet, Primary Election, June 6, 1978.* In that regard, Proposition 5 made specific the separation of powers stated in Article III, section 3, of the Constitution, between the legislative and executive branches on the one hand and the judicial branch on the other as to the review of statutes.

I am aware of no similar restriction on the exercise of quasi-judicial power as to regulations. To the contrary, in *Woods v. Superior Court* (1981) 28 Cal.3d 668, the California Supreme Court unanimously held that applicants could challenge the validity of a Department of Social Services regulation at the administrative hearing stage. Quite simply, administrative hearings before OTA are adjudicatory in nature and a challenge to the validity of a regulation is cognizable in such hearings. *See Harris Transportation Co. v. Air Resources* Board (1995) 32 Cal.App.4th 1472, 1479 (challenge to regulation can be made in agency's adjudicatory enforcement proceedings).

Significantly, BOE, OTA's predecessor, itself considered the validity of regulations. In *Appeal of Save Mart Supermarkets & Subsidiary* (2002-SBE-002) (2/6/2002), the BOE exercised its quasi-judicial powers and found a regulation invalid. OTA not only holds the quasi-judicial powers formerly held by the BOE in hearing appeals from FTB actions (and post-June 30, 2017, in hearing business tax appeals) but also, by being vested with all of the duties, powers, and responsibilities of the BOE relative to hearing appeals, has been granted those quasi-judicial powers by the Legislature. Gov't Code §§ 15672(a) and 15674(a)(1). There is nothing in statute or the Constitution to limit OTA's review of regulations of other agencies in the course of hearing tax appeals as OTA proposes.

Moreover, if, by proposing this amendment disavowing its quasi-judicial power to decide issues presented concerning regulations of other agencies, OTA is seeking to preemptively decide (or preemptively avoid deciding) parts of several, if not more, pending cases, that is improper in and of itself. The Director is statutorily prohibited from being involved in the decision-making process of the tax appeals panels. Yet the adoption of regulations is within the Director's purview, and the rulemaking process in this regard potentially interferes with the decision-making process in pending cases. Indeed, even the drafting and release of the proposed amendment may be prejudicial to pending cases.

Questions related to the validity of regulations issued by other agencies may come up from time to time in the ordinary course of tax appeals as to which OTA holds quasi-judicial power. Yet OTA proposes to avoid such questions, even though an invalid regulation is unenforceable, and instead

require appellants to abandon all such questions or take them to court. OTA should not take it upon itself to decide through a procedural regulation questions that impact appellants' substantive rights.

6. Section 30104 (Limitations on Jurisdiction): The proposed amendment adding new subsections (e)(2) and (3) proposes to disavow jurisdiction where a taxpayer did not receive certain procedural rights during the audit or internal appeal process at the California Department of Tax and Fee Administration ("CDTFA"). Inasmuch as the existing regulation only gave an example for FTB matters, I realize these proposed new subsections are intended as examples for CDTFA matters which OTA believes would not impact "the adequacy of a notice, the validity of an action from which a timely appeal was made, or the amount at issue in an appeal." I would caution, as I am sure you have seen, that not every appellant fully articulates their concern or uses precise language and sometimes a taxpayer may state their complaint in a way that appears to fall outside OTA's jurisdiction as stated in (e) and yet may be within. I would hope that OTA's internal review analyzes a taxpayer's submission to avoid unduly rejecting appeals based on imprecise or poorly worded requests in case there is something there.

7. Section 30202 (Time for Submitting an Appeal): I do not have a comment at this time on your proposed amendments. However, in reading through the document, I noticed that (a)(1) refers to "unpaid assessments." This appears to be a colloquial use of the word "assessment." If a taxpayer timely appeals from a notice of action of a protest of a proposed assessment, there has been no assessment; the assessment is still proposed. A taxpayer may choose to make a deposit (not recorded as a payment). Or a taxpayer may pay a proposed assessment during the pendency of the protest or appeal, which converts the protest or appeal into a claim for refund per Rev. & Tax. Code § 19335.

8. Section 30203 (Time for Submitting an Appeal): In subsection (b) regarding appeals from an action of CDTFA, you simplified certain references by deleting "CDTFA" before "Appeals Bureau" in the numbered subsections, leaving only the main reference in the introductory portion. Two references were missed in making the global change. In (b)(3), the corresponding change would be from "If CDTFA's Appeals Bureau" to "If the Appeals Bureau . . ."; and in (b)(4), the corresponding change would be from "after CDTFA's Appeals Bureau" to "after the Appeals Bureau."

9. Section 30210 (Conferences): The proposed amendments to subsection (e) change "reasonable notice" to "written notice" in the first sentence, delete "reasonable" from "reasonable written notice" in the last sentence and, in a rearranging of the current regulation, provide that OTA will consult with the parties on scheduling conferences other than prehearing conferences. I can only assume that OTA's proposal to delete "reasonable" and not provide any requirement for the timing of the notice of a conference is because OTA will consult with and obtain agreement from the parties as to the place, date and time of conferences. However, that would not apply to prehearing conferences inasmuch as OTA does not consult, or at least is not required by the regulation to consult, with the parties on the scheduling of a prehearing conference. The net result is that there appears to be no requirement as to how much notice OTA must give of a conference and in particular of a prehearing conference.

10. Section 30211 (Representation): With respect to subsection (c) "Local entity representation," a waiver from the taxpayer allowing a representative to have access to confidential taxpayer information is not necessary when the representative has a Rev. & Tax. Code § 7096(b) resolution from the local entity they represent. Access to confidential taxpayer information is a provided by the statute for a representative that has a Rev. & Tax. Code § 7096(b) resolution. Unless the taxpayer joins the appeal as a party, a waiver from the taxpayer is necessary for the representative to have access to confidential taxpayer information when the representative does not have a Rev. & Tax. Code § 7096(b) resolution, but instead has a power of attorney from or a written contract with the local entity they represent. However, the phrasing of the current regulation appears to require a waiver from the taxpayer even when the representative has a Rev. & Tax. Code § 7096(b) resolution, as it requires (1) a resolution or power of attorney from, or written contract with, the local entity "and" (2) a waiver from the taxpayer. I suggest the provision be clarified as follows: "Notwithstanding subdivision (b), and within 30 days of OTA's letter acknowledging the appeal, OTA must be provided with: (1) a copy of the resolution or power of attorney from, or a written contract with, the local entity they represent authorizing their representation; and (2) if the representative does not have a resolution, a copy of a waiver from the taxpayer allowing each representative to have access to the taxpayer's confidential information. If the taxpayer joins the appeal as a party, then no waiver is required." This suggestion simply clarifies the situations in which a waiver is needed using the language of the existing regulation. However, in fact, the absence of a waiver should only preclude the representative from receiving confidential taxpayer information related to the appeal and not adversely impact the representative's authority to represent the local entity before OTA. This distinction could be recognized by placing the authorization of representation and the access to confidential taxpayer information in separate sentences, much as CDTFA's Regulation 35056(b)(2) places them in separate subparagraphs.

11. Section 30219 (Application of Burden of Proof): The proposed amendment rightly places the burden of proof with respect to a new matter raised by the respondent (typically FTB or CDTFA) on the respondent. The proposed amendment errs, however, in restricting new matters to those that would increase the liability at issue (generally not possible since the period for proposing a deficiency would have passed) or result in an offset (generally happens when the liability cannot be increased as the period for proposing a deficiency has passed). OTA would encourage sandbagging and shifting positions by the tax agencies, regardless of consistency with the tax agency's original position, thereby prejudicing taxpayers who have not developed the facts necessary to defend against new assertions or theories/arguments by the tax agency on which OTA would nevertheless have the taxpayer bear the burden of proof. As stated by the BOE in *Appeal of Sierra Pacific Industries* (94-SBE-002) (1/5/1994): "If respondent's position on appeal results in a larger deficiency (had respondent adopted it initially), or requires the presentation of different evidence, then a new matter has been introduced and the burden of proving that new position shifts to respondent. However, the assertion of a new theory that merely clarifies or develops the original determination without being inconsistent with it or increasing the amount of the deficiency, it is not a new matter requiring the shifting of the burden of proof to respondent [citing *Appeal of Mendelsohn* (85-SBE-141) (11/6/1985) and other cases]." For example, where FTB had asserted a deficiency on grounds that stock had not been acquired after September 16, 1981, and argued for the first time on appeal that the taxpayer should not prevail because the stock was

not small business stock, the new theory FTB raised to support the deficiency was a new matter that required the presentation of different evidence than that required to resolve the issue originally raised by FTB in asserting the deficiency and thereby shifted the burden of proof to FTB. *Appeals of George and Linda Barry, et al.* (93-SBE-006) (4/22/1993). OTA itself has recognized that "new matter" includes one "which requires the presentation of different evidence." *Appeal of Praxair, Inc.* (2019-OTA-301P) (10/3/2019) at 10-13 (adopting standard from *Appeal of Mendelsohn* and finding CDTFA failed to meet its burden); *Appeal of MJK Real Estate Fund II, LLC* (2022-OTA-247P) (5/26/2022) at fn. 34 (stating principle and citing *Appeal of Mendelsohn*); *Appeal of B.B.C.A.F., Inc.* (2019-OTA-275) (9/6/2019) at 11-15 (new matter was raised where different evidence was required and FTB failed to raise the new alternative position in its notice of proposed assessment). The proposed amendments should make clear that a new matter includes one that is inconsistent with the position taken in making the original determination or that requires the presentation of different evidence; that the tax agency cannot, without bearing the burden of proof, raise new theories that do not simply clarify or develop their original position, but that instead require a different factual basis or rationale.

12. Section 30220 (Postponement and Deferral): The proposed amendments would delete as an example of good cause that "all parties desire a postponement." This deletion should be reinstated. It does not make sense that OTA would force parties to a tax dispute to proceed when the parties are in agreement that a postponement is warranted, even if they each agree for their own reasons.

13. Section 30223 (Dismissal): The proposed amendment adding new subsection (g) would provide for the dismissal of an appeal where "a party fails to respond, ceases to participate, or otherwise is non-responsive during the appeals process." Presumably OTA is seeking to have a regulation that addresses particular circumstances it has faced and provides a process to deal with a perceived problem. An appellant should not be prejudiced if the failure is on the part of the tax agency (or another party), yet dismissal of the appeal in such circumstances would prejudice the appellant since dismissal would leave the tax agency's determination standing. In addition, included as a possible failure to participate that might result in dismissal of the appeal is "an Agency concession or withdrawal from an appeal without timely notifying OTA." Again, dismissal could prejudice the appellant because there is no guarantee that the Agency will have processed its concession or withdrawal and the possibility remains that the dismissal will result in the Agency's original determination being processed as final. At the least, any such dismissal should acknowledge the Agency's concession or withdrawal so that the action of OTA reflects the true status of the dispute.

14. Section 30224 (Request for Reconsideration of an Appeals Bureau Decision): "CDTFA's Appeals Bureau" in the added language in (a) and at the beginning of the text in (b) should be "the Appeals Bureau."

15. Section 30401 (Process for Requesting an Oral Hearing): Proposed new subsections (d) and (e) would provide for forfeiture of the right to an oral hearing under certain circumstances, while proposed new subsection (f) would provide for review of any forfeiture decision by the Chief Counsel. It appears OTA may be trying to address particular circumstances it has faced or speculates that it might face in the

future. Forfeiture or deemed waiver of the right to an oral hearing is an extreme remedy that should be avoided. It is possible that the circumstances described in subsection (d), that a party's presence at an oral hearing may threaten the health or safety of any person present, could be solved short of denying the party's right to an oral hearing, depending on the circumstances. A virtual oral hearing could be held. If the situation is one, e.g., where one spouse has a protective order against, or is in fear of, the other spouse, separate hearings could be held or the spouses could be kept separate during the course of the hearing. Perhaps subsection (d) is meant to address a situation that arises during the course of the hearing itself. Certainly, OTA could stop the hearing, clear the disruptive individual from the room and provide protection to the threatened individual(s) in the face of a threat to health and safety. I do acknowledge, however, that a person's health or safety may be threatened by another person even in a virtual oral hearing. My point is simply that the proposed subsection (d) is stated in the absolute ("an appellant forfeits the right to an oral hearing") even though situations differ, and that the particular circumstances need to be considered, including whether an alternative path for providing the oral hearing exists. Perhaps that is where proposed subsection (f) comes in. Indeed, subsection (f) indicates that the forfeitures under subsections (d) and (e) are meant to be only forfeiture of an in-person oral hearing. If so, the reference in each of those subsections to "forfeiture of the right to an oral hearing" should be changed to "forfeiture of the right to an in-person oral hearing." Finally, it is unclear that proposed new subsection (e) is even necessary inasmuch as postponements and reschedulings generally require good cause. Without an explanation of what caused OTA to draft these proposed amendments, they seem to be a solution in search of a problem.

16. Section 30501 (Publication of an Opinion): Proposed new subsection (g) states that where a petition for rehearing is granted, the Opinion on Petition for Rehearing shall be published in addition to the Opinion on Rehearing. However, proposed new subsection (g) further states that OTA will also publish the superseded Opinion. That provision should be deleted. Superseded Opinions should not be published. They are not the final action in the appeal. Publication of superseded Opinions is not required by statute. Government Code § 15674(a)(2) requires OTA to issue a written opinion for each appeal decided. A superseded opinion does not represent OTA's decision. Publication of superseded Opinions does not advance the body of administrative law and could lead to confusion and potential prejudice in other cases. Proposed new subsection (h)(2) regarding the numbering of superseded Opinions should correspondingly be deleted.

17. Section 30502 (Process for designating an Opinion as Precedential): Consistent with the comment above, delete the reference to Superseded Opinions in proposed new subsection (f).

18. Section 30608 (Effect of Withdrawal or Failure to Participate During a Petition for Rehearing): Please see comments above re Section 30223 (Dismissal) as they apply also to proposed subsection (e) of this proposed new regulation. In addition, the last sentence of proposed subsection (e) states OTA may dismiss an appeal, which would be improper inasmuch as the subsection concerns the petition for rehearing not the underlying appeal. The reference to dismissing an appeal, rather than a petition for rehearing, appears to be an editing/proofreading error.

Please contact me if you have any questions or would like to discuss these initial comments.

Sincerely,

Marcy Jo Mandel

cc: Charles J. Moll III

March 16, 2023

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Submitted electronically: regulations@ota.ca.gov

RE: Interested Parties Meeting to discuss Proposed Amendments to Rules for Tax Appeals

To Whom it May Concern,

Thank you for the opportunity to comment on The Office of Tax Appeals' (OTA) proposed amendments to its Rules for Tax Appeals. The California Chamber of Commerce is concerned about the potential negative impacts that could result if these amendments are instituted.

The California Chamber of Commerce ("CalChamber") is a non-profit business association with approximately 14,000 members, both individual and corporate, representing 25% of the state's private sector and virtually every economic interest in the state of California. While CalChamber represents several of the largest corporations in California, 70% of its members have 100 or fewer employees. CalChamber acts on behalf of the business community to improve the state's economic and jobs climate by representing business on a broad range of legislative, regulatory, and legal issues.

Specially, we write with concern regarding the Jurisdictional Limitations contained within Regulation 30104. This section would limit the jurisdiction of the OTA in cases that challenge the validity of a regulation contained within Regulation 30104(d) and 30104(e). Under the current regulations, the OTA is allowed to comment on the validity of a regulation as it applies to an appeal. The practical application of the proposed amendment being implemented would mean a taxpayer potentially having an assessment before the OTA where that taxpayer cannot challenge the validity of the tax regulation. Thus, a taxpayer would be forced to handle the assessment before the OTA then pay for separate litigation within the court system to address the Regulation's validity rather than adjudicating all issues to finality in front of the OTA.

This is of concern because there is nothing in the current statutes that limits jurisdiction. The current statutes are based largely on historical guidance in legislative history and the Board of Equalization (BOE). When the BOE was permitted to hear appeals, the Board had the jurisdiction to hear challenges to regulations.

Additionally, this change to the regulation would limit the authority on audit exit conferences, remove the quasi-judicial power of the OTA and create a body of non-Constitutional officers, make the outcome of pending litigation unknown leading to uncertainty of the transfer of pending cases, and create an inaccessible appeals process for pro se appeals.

Thank you for your consideration of our perspective.

Sincerely,

Preston Young
Policy Advocate

PY:ldl

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March 20, 2023

Mr. Mark Ibele
Director
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Sent Via Email

Re: Comments in Response to Proposed Amendments to the OTA's Rules for Tax Appeals

Dear Director Ibele,

Thank you for the opportunity to provide feedback in response to the proposed amendments to the Rules for Tax Appeals released by the Office of Tax Appeals (OTA) in February 2023. The forum that the OTA provides for taxpayers and other interested parties to respond to potential changes in the adjudication of California's tax laws is always welcomed.

The California Taxpayers Association (CalTax) would like to provide comments regarding certain proposed amendments to the Rules for Tax Appeals ("Rules") and address areas of concern where the proposed amendments could cause the OTA to depart from its core role in fairly resolving tax disputes and appeals among taxpayers and government agencies.

CalTax was established in 1926 as a nonpartisan, non-profit tax research and advocacy association, and is the state's largest and oldest organization representing California taxpayers. Its mission is to promote sound tax policy and government efficiency. CalTax members include individuals, small businesses and Fortune 500 companies operating in every sector of the California economy.

Jurisdictional Limitations

CalTax's most significant concern involves proposed changes to Section 30104 of the Rules that would materially limit the jurisdiction of the Office of Tax Appeals to hear and adjudicate certain tax appeal issues. These changes would significantly truncate the role of the OTA and inappropriately limit the ability of taxpayers to have important tax issues adjudicated without going to court. These proposed jurisdictional changes include the following:

- Section 30104(d): The proposed amendments state that the OTA does not have jurisdiction to determine whether "a provision in the California Codes of Regulations is

invalid or unenforceable, or whether OTA may otherwise refuse to follow an applicable provision in the California Code of Regulations, unless a federal or California appellate court has already made such a determination." This limitation would include issues involving (i) whether a Tax Agency's regulation conflicts with the Revenue and Taxation Code, and (ii) whether a regulation conflicts with another regulation of the Tax Agency.

- The proposed amendments also create further limits on jurisdiction in Section 30104(e), which are discussed below under the Fundamental Fairness section.

With regard to the Section 30104(d) amendments, the OTA's current Rules for Tax Appeals do not limit the OTA's jurisdiction to determine the validity of a regulation, and the proposed amendments represent a sea change in the California tax appeals process. If the proposed amendments were to be implemented, a taxpayer would have to file a lawsuit in court to challenge the validity of a tax agency regulation.

CalTax respectfully asserts that the proposed language in Section 30104(d) limiting jurisdiction with respect to the validity of tax agency regulations conflicts with California law. The OTA's powers are defined in Government Code Section 15672, which states that the OTA "is the successor to, and is vested with, all of the duties, powers and responsibilities of the Board of Equalization necessary to conduct appeal hearings." Thus, for taxpayer issues determined by the Franchise Tax Board (FTB) and the California Department of Tax and Fee Administration (CDTFA), the OTA succeeded to the jurisdictional authority that existed in the Board of Equalization. The Board of Equalization long exercised its power to determine the validity of tax regulations promulgated by other tax agencies in important Board decisions. Prominent examples include *Appeal of Standard Oil Company of California*, decided March 2, 1983 [83-sbe-068], and *Appeal of Save Mart Supermarkets & Subsidiary,* decided February 6, 2002 [2002-sbe-002]. In *Standard Oil,* the Board determined that FTB Regulation Section 25120(c)(4) (concerning the treatment of dividends as nonbusiness income) was invalid because it was inconsistent with Revenue and Taxation Code Section 25120(a). In *Save Mart*, the Board determined that FTB Regulation Section 23649-3 (concerning whether appellant was a "qualified taxpayer" eligible for the Manufacturers' Investment Credit) was invalid because it was inconsistent with Revenue and Taxation Code Section 23649(c)(1).

Nothing in the statutory language enacting the OTA, nor in the legislative history thereunder, states or suggests that the OTA lacks jurisdiction to determine the validity of tax agency regulations. As noted, Government Code Section 15672 instead states affirmatively that the OTA shall carry on with the powers vested in the State Board of Equalization, which includes the

power to determine the validity of regulations. Similar language is reiterated repeatedly in the legislative history underlying the OTA statutes.[1]

It is not clear what authority the OTA relies on for this limitation on jurisdiction in the proposed Rules because a detailed whitepaper was not provided with the proposed language.

However, a recent OTA precedential opinion in *Appeal of Alfredo J. Talavera*, 2020-OTA-022P, relied solely on Government Code Section 11350 for the conclusion that the OTA does not have authority to invalidate a regulation. The *Talavera* opinion stated:

> In California, only a court may declare a quasi-legislative regulation that has been formally promulgated by a state agency, such as Regulation 1642, to be invalid. (Gov.Code, Sec. 11350(b).) Therefore, OTA does not have authority to declare Regulation 1642 invalid and refuse to follow it on that basis.

However, Government Code Section 11350 only provides an affirmative grant of authority to seek invalidation of a regulation in court, stating that "[a]ny interested person may obtain a judicial declaration as to the validity of any regulation or order of repeal by bringing an action for declaratory relief in the superior court in accordance with the Code of Civil Procedure." Section 11350 does not state that this is the only situation where a regulation may be invalidated and does not address the authority of the OTA or any other appeals body to invalidate a regulation. Respectfully, Section 11350 is a very slender reed to rely on in implementing a major change to California's tax appeal process, particularly given the long history of the Board of Equalization handling issues involving the validity of regulations.

Moreover, from a tax policy perspective, excluding the OTA from determining the validity of regulations promulgated by the state tax agencies would unfairly favor the agencies at the expense of taxpayers. Taxpayers would be forced to pay the tax and file a complaint in court to challenge the validity of a regulation, which would put a huge financial and time burden on taxpayers, particularly small businesses and *pro se* appeal taxpayers. Very few tax issues are material enough to justify court litigation, and very few taxpayers have the resources to pursue a court case. This "cost of litigation" impact would trickle down to protests and settlements, where the tax agencies could adopt aggressive postures on suspect regulations knowing that the regulations could be challenged only in the rarest of instances. This contradicts California's goal to apply a fair and efficient process to collect taxes, as discussed below.

[1] For example, please see sections 2(e) and 23 of Assembly Floor Analysis for AB 102 (2017), attached.

Fundamental Fairness

With due respect to the complexities of crafting these new rules, certain aspects of the proposed amendments project an air of unfairness toward taxpayers that we recommend be modified or eliminated. In addition to the discussion above, other examples include the following provisions:

- New examples in Regulation 30104(e) limit the jurisdiction of the OTA in cases where a Tax Agency fails to follow its own audit or appeal procedural rules to the detriment of the taxpayer. At a minimum, this sends an insensitive message to the taxpayer community that the Tax Agencies can ignore their own procedures without consequence. More importantly, these types of situations *should* be eligible for OTA jurisdiction because an Agency's failure to follow its own procedures could prevent the correct determination of tax liability under the law.

    - By way of example, the FTB has robust procedures in place to approve Revenue and Tax Code Section 25137 alternative apportionment variances. Per the FTB Audit Manual, these procedures apply to auditors as well as taxpayers, and auditors are required to go through layers of approval before imposing an alternative apportionment variance. There have been instances where auditors have not followed these approval procedures and imposed proposed assessments. This type of error is not merely a procedural lapse, but goes to the fundamental determination of the correct tax liability, and should be an issue that the OTA has jurisdiction to consider.

- Proposed amendments in Regulations 30223(g) and 30608 allow the OTA to dismiss an appeal if a party ceases to be responsive or appropriately participate in the appeal proceedings. However, this appears to be limited solely to the taxpayer/appellant and similar consequences are not imposed on a Tax Agency that is nonresponsive or does not participate appropriately in the appeal proceedings. Fairness dictates that there should be similar consequences for both parties in situations where the parties cease to be responsive or participate appropriately in the proceedings.

- In support of these points, we repeat relevant language from the California Taxpayers' Bill of Rights:[2]

[2] Rev. & Tax Code Section 7081.

- The Legislature finds and declares that taxes are the most sensitive point of contact between citizens and their government, and that there is a delicate balance between revenue collection and freedom from government oppression. It is the intent of the Legislature to place guarantees in California law to ensure that the rights, privacy, and property of California taxpayers are adequately protected during the process of the assessment and collection of taxes. (Emphasis added.)

- The Legislature further finds and declares that the purpose of any tax proceeding between the State Board of Equalization and a taxpayer is the determination of the taxpayer's correct amount of tax liability. It is the intent of the Legislature that, in furtherance of this purpose, the State Board of Equalization may inquire into, and shall allow the taxpayer every opportunity to present, all relevant information pertaining to the taxpayer's liability.

Thank you for the opportunity to comment on these proposed amendments. Please don't hesitate to reach out.

Sincerely,

Bart Baer
Chief Tax Counsel
California Taxpayers Association

CC: Dee Dee Myers, Director of Governor's Office of Business and Economic Development
Luis Larios, Deputy Secretary of Legislation & External Affairs, Government Operations Agency
Jiwon Jeong, Deputy Secretary & Attorney IV for Tax Matters, Government Operations Agency
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March 20, 2023

SENT VIA E-MAIL (REGULATIONS@OTA.CA.GOV)

Office of Tax Appeals
P.O. Box 989880
West Sacramento, CA 95798-9880

Re: Comments Regarding Proposed Amendments to Office of Tax Appeals Rules for Tax Appeals

Thank you to the Office of Tax Appeals ("OTA") for holding the Interested Parties Meeting ("IPM") on March 20, 2023, regarding the proposed amendments to the OTA Rules for Tax Appeals. We appreciate the opportunity to voice our concerns with the newly revised language in the proposal.

I. Response to OTA's Proposed Regulations

We have a number of concerns regarding the OTA's proposed amendments, which will be detailed below in the first section of our comments.

a. Regulation section 30104 – Limitations on Jurisdiction

We have a significant concern regarding OTA's proposed amendments to Regulation section 30104, relating to OTA's proposed new self-limitation on its jurisdiction. We currently have a case pending before OTA that tangentially involves a question of whether OTA can determine whether a regulation contained in the California Code of Regulations is invalid based on the fact that it conflicts with another regulation contained in the California Code of Regulations and promulgated by the same agency. We are also aware of other pending cases regarding similar types of issues.

There is a significant issue that the proposed amendment being put forth by OTA is influencing pending decisions and appeals and does bias the ALJs in deciding current cases involving the OTA's jurisdiction to determine the validity or invalidity of a regulation. Furthermore, we emphatically disagree that OTA lacks jurisdiction to decide whether a regulation is invalid or unenforceable. Per Government Code section 15672:

> "(a) Except as provided in subdivision (b) of Section 15600, the office is the successor to, and is vested with, all of the duties, powers, and responsibilities of the State Board of Equalization necessary or appropriate to conduct appeals hearings."

It is undisputed that the State Board of Equalization ("BOE") had the authority to determine the validity of a regulation, both in regard to any potential conflict with the Revenue and Taxation Code and with respect to another regulation. As the OTA stepped into the shoes of the BOE as a

result of AB 102 in 2017, the OTA clearly has the authority to determine the validity or invalidity of a regulation vis-à-vis statutes and other regulations.

In addition, we are also troubled by the proposed language in Regulation section 30104 (e)(2) and (3). It is ludicrous that taxpayers are required to comply with all of the relevant laws and regulations, but CDTFA does not have to do so and OTA is attempting to limit whether it can decide whether a taxpayer may be entitled to relief on the basis that the agency failed to follow its own audit procedures. This will be a huge burden for taxpayers.

Where is the fairness and level playing field? Under this new amendment, taxpayers will be forced to pay the tax, and then bring suit in superior court for a refund. This seems incredibly onerous, as taxpayers will face increased costs for litigation, in addition to having to pay the disputed liability upfront to just get into court. To add insult to injury, even if the taxpayer is able to succeed in court, the tax agencies' credited interest rates are minimal to non-existent. The proposed new revisions to this section of the regulation are fundamentally unfair because it essentially bestows free reign for tax agencies to disregard their own audit procedures with no recourse, and taxpayers would face serious difficulty to obtain any form of relief.

Regulation section 1698.5, Audit Procedures, states in section (b), "This regulation provides taxpayers and Board staff with the necessary procedures and guidance to facilitate the efficient and timely completion of an audit. The regulation also provides for appropriate and timely communication between Board staff and the taxpayer of requests, agreements, and expectations related to an audit." This goes to the heart of determining the correct amount of tax. The procedures outlining the required interactions between taxpayers and CDTFA staff ensure that both parties have the documents necessary to determine the amount of tax and resolve any disagreements regarding that amount. In addition, section (b)(4) outlines the duty of Board (CDTFA) staff. In this section, the regulation states that the duties of Board staff include the following:

> (A) Apply and administer the relevant statutes and regulations ***fairly and consistently*** regardless of whether the audit results in a deficiency or refund of tax.
> (B) Consider the materiality of an area being audited. Audit decisions are based on ***Board staff's determination of the amount of potential adjustment*** balanced against the time required to audit the area and the duty to determine ***whether the correct amount of tax has been reported.***
> (C) Make information requests for areas under audit as provided in Regulation 1698. The auditor will explain why records are requested when asked to do so. The auditor will also work with a taxpayer to resolve difficulties a taxpayer has when responding to Board information requests, including the use of satisfactory alternative sources of information....

The regulation continues explaining the additional duties of Board staff, and also the duty of taxpayers, which include maintaining records and documents. Again, these types of issues speak precisely to determining the correct amount of tax included in CDTFA assessments. The audit procedures provide guidelines for an agency to resolve the fundamental question of the correct amount of tax, and an agency's failure to follow those procedures undoubtedly affects that determination. Thus, OTA must examine and ascertain whether the appropriate procedures were followed in order to make any conclusion as to whether the amounts at issue in the appeal are accurate.

Moreover, as stated in the Assembly floor analysis for AB 102, "the proposal upholds the "Taxpayers" Bill of Rights" by ensuring taxpayers are protected during the process of fair assessment and collection of taxes."

In 1988, the Taxpayers' Bill of Rights was enacted to ensure that the "rights, privacy, and property of California taxpayers are adequately protected in the assessment and collection" of sales and use taxes. The Taxpayers' Bill of Rights recognizes "that taxes are the most sensitive point of contact between citizens and their government, and that there is a delicate balance between revenue collection and freedom from government oppression." Furthermore, the statute provides additional language regarding the Legislature's intent for the law stating, "It is the intent of the Legislature that, in furtherance of this purpose, the State Board of Equalization may inquire into, and shall allow the taxpayer every opportunity to present, all relevant information pertaining to the taxpayer's liability." This proposed amendment goes against that legislative intent, as it would diminish the rights and ability of taxpayers to pursue recourse and present evidence regarding improper audit conduct.

If OTA wants to tie its hands regarding these types of issues, it should go through the appropriate process of seeking legislative amendments to its granted authority and limit its jurisdiction. Otherwise, the OTA's proposed amendments to Regulation section 30104 are impermissibly narrowing Government Code section 15672.

II. Suggested Additions to OTA's Proposed Regulations

We also have some proposed additions to the OTA's proposed amendments. It is our view that if OTA is opening up the regulatory process for their proposed amendments, potential additions to improve the regulations should also be reviewed. Some of those potential additions are discussed in detail in the section below.

b. Regulation section 30411 – Disqualification for Cause

The OTA did make some positive changes in Regulation section 30411 to add that not only can Panel Members be disqualified for cause, but also that any other member of OTA's legal division who is assigned to work on an appeal may also be disqualified. However, we think the disqualification for cause should also extend to non-legal staff, or "super auditors" who may be working on appeals. Our suggested change would be to delete the reference to OTA's legal division and instead allow a motion to disqualify to apply to any other member of OTA.

> Any party may file a motion to disqualify for cause any Panel Member or any other member of OTA~~'s legal division~~ who is assigned to work on an appeal, based upon the grounds set forth in Government Code sections 11425.30 to 11425.40, or upon any other basis required by law. There is no right to peremptory challenges.

c. Regulation section 30104.5 – Penalties

We have seen in a number of cases that OTA has been overly harsh in regard to imposing penalties on taxpayers. For example, the OTA's decisions regarding the demand penalty under Regulation section 19133. A new section addressing penalties will be constructive in shaping a reasonable OTA approach to reviewing the imposition of penalties.

> 30104.5 **Penalties**
>
> (a) In general, the imposition of penalties under the Revenue and Taxation Code are intended to encourage voluntary taxpayer compliance and are not intended as a punitive measure. The imposition of a penalty is discretionary based on individual

facts and circumstances. OTA has the discretion to determine whether a penalty was properly imposed, and overturn the imposition of any penalty made under the Revenue and Taxation Code. Whenever there is any doubt as to whether factual conditions warrant a penalty, that doubt should be resolved in favor of the taxpayer.

d. Regulation section 30214 – Evidence

We have a major concern with the failure of the ALJs to properly weigh evidence admitted into the record. Based on our experience working on several appeals before OTA, we also have some suggested language below for Regulation section 30214(f) that further makes clear OTA's responsibility in taking evidence and weighing that evidence fairly and consistently.

(4) The Panel may use the California rules of evidence when evaluating the weight to give evidence presented in a proceeding before OTA. The OTA shall consider, the degree of persuasiveness and reliability of any evidence presented. Any party may provide argument on the relevant weight that should be given to an item of evidence.

(5) After weighing the evidence, the Panel ~~may~~ shall make factual findings in any Opinion issued by OTA. A factual finding on any material disputed fact shall not be based solely on unsworn statements made by a party during the appeal proceeding before OTA, such as statements contained in a party's brief, or arguments made by an unsworn representative during an OTA oral hearing. However, a factual finding on any material disputed fact shall be based on sworn statements made by a party during the appeal proceeding before OTA, such as testimony by a sworn witness during an OTA oral hearing, or signed declarations submitted by a party.

We have had cases where the OTA has failed to consider or weigh relevant evidence. We believe the OTA must be compelled in its regulations to weigh and consider all relevant evidence. The local Assessment Appeals Boards for property tax appeals have similar language that obligates the board to consider the evidence and such language is correspondingly appropriate for the OTA.

Again, the Taxpayers' Bill of Rights was intended to ensure that "the State Board of Equalization may inquire into, and shall allow the taxpayer ***every opportunity to present, all relevant information*** pertaining to the taxpayer's liability." As the successor to the Board for tax appeals, OTA must not only allow taxpayers to present all relevant information but also appropriately consider and weigh the evidence.

e. Regulation section 30436 – Panel Selection Process

We believe that amendments to this section are needed, given the legislative change to allow non-attorneys to participate on an OTA panel.

In our view, one necessary change as a result of that legislative change is to further add a section to this section to state that:

(b) If a pending appeal before the OTA solely involves a question of law, the panel shall be comprised solely of administrative law judges. If a pending appeal involves both questions of law and other issues, such as audit methodology, a party shall have the right to petition that the panel is comprised solely of administrative law judges. The OTA shall grant such a petition unless it can specify in writing a reasonable basis why it is not feasible to do so.

This language can address potential concerns that non-attorneys will be deciding legal issues without the necessary expertise and proficiency required to conduct legal analysis. Questions of law are necessarily nuanced and complicated, and this is especially true in tax law. Panels comprised of non-attorneys making determinations on legal issues will certainly lead to an increase in erroneous decisions, as even presently, OTA panels comprised entirely of ALJs have, on occasion, issued incorrect opinions contrary to law.

f. Regulation section 30504 – Precedential Opinions of the Board of Equalization

Longstanding BOE opinions must be followed. If OTA considers depublishing a precedential BOE opinion, the public should be able to comment before the removal of the precedential status of a BOE opinion. We would suggest adding the below language to OTA's Rules for Tax Appeals because it protects the well-settled laws that Californians may have reasonably relied upon.

> Before removing the precedential status of an opinion of the State Board of Equalization, the OTA shall specify the reasons why it is removing such precedential status, and allow a thirty (30) day period for the public to submit comments before the OTA makes a final determination on the removal of the precedential status of a BOE opinion.

We request the OTA hold a second IPM before moving forward to the formal regulatory process at the Office of Administrative Law because of the volume and significant nature of the new amendments proposed by OTA.

Thank you again for the opportunity to provide input. Please telephone if you have any questions whatsoever.

Very truly yours,

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20 March 2023

To: Office of Tax Appeals
From: Dan Kostenbauder, VP Tax Policy
Re: Proposed Amendments to Rules for Tax Appeals

The Silicon Valley Leadership Group appreciates the opportunity to provide input with regard to proposed amendments to the Office of Tax Appeals (OTA) Rules for Tax Appeals (Rules).

SVLG's major concern with the proposed amendments to the Rules is with section 30104(d), which imposes limitations on the jurisdiction of the OTA that are not required by statute, and are in fact contrary to statute.

The legislation creating the OTA clearly expected that the OTA would step into the role of the State Board of Equalization with regard to resolving tax controversies. Paragraph 23 of the Assembly Floor Analysis for the Taxpayer Transparency and Fairness Act of 2017 "States that the OTA is the successor to, and vested with, all the duties, powers, and responsibilities of the Board necessary or appropriate to conduct appeal hearings not related to the responsibilities listed in numbers 3 and 4." 201720180AB102_Assembly Floor Analysis.pdf

The State Board of Equalization exercised its authority to decide cases based upon its determination that regulations of the Franchise Tax Board were invalid. See, for example, Save Mart Supermarkets 2002-SBE-002.

The OTA should not promulgate amendments to the Rules that limit its authority to declare regulations invalid on the same basis as the State Board of Equalization did. To do so would be contrary to the expectations of the Legislature in creating the OTA.

The OTA has an important role in resolving controversies between taxpayers and the Franchise Tax Board (FTB) and California Department of Tax and Fee Administration (CDTFA). By limiting the OTA's jurisdiction to resolve a dispute in favor of a taxpayer in a situation where the FTB or CDTFA regulations exceed their statutory authority or conflict with other regulations, the proposed amendments to the Rules will force taxpayers to expend time and resources to go to court when they should not need to do so. Furthermore, if the proposed Rules are adopted, there would be less constraint on Agencies adopting regulations that go beyond their statutory authority.

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The authorities cited in support of the amendments to section 30104 Limitations on Jurisdiction do not, in fact, support the proposed limitations on the jurisdiction of the OTA in section 30104(d). For example, section 15679.5 of the Government Code was cited, but paragraph 15679.5(b)(3) refers to the Model State Administrative Tax Tribunal Act ("Model Act"), under which the proposed limitations on OTA's jurisdiction would not be valid. Section 7(A) of the Model Act states that "the Tax Tribunal [OTA] shall be the sole, exclusive and final authority for the hearing and determination of questions of law and fact arising under the tax laws of this State." That broad statement of authority would surely allow the OTA to invalidate an Agency regulation because it is inconsistent with a statute or other regulation. Section 7(E) would limit the jurisdiction of the OTA by not allowing the OTA to declare a statute unconstitutional, which is a much different restriction than the proposed amendments would make by not permitting the OTA to determine that an Agency regulation is invalid because it conflicts with a provision of the Revenue and Taxation Code or another regulation.

Two court cases are also cited as authority for the Limitations on Jurisdiction in proposed amendments to section 30104 of the Rules. These cases do not preclude the OTA from having jurisdiction to find regulations of the tax Agencies invalid. *People ex rel. Lynch v. Superior Court* holds that the court will not issue advisory opinions. Clearly a case before the OTA brought by a taxpayer would call for an opinion with consequences, not just an advisory opinion. *Newco Leasing, Inc. v. State Board of Equalization* has language stating that the ***ultimate*** (emphasis added) determination whether the Board correctly interpreted the statutes and its regulations rested with the courts, but it did not preclude the Board from making such determinations. Of course, the Board would hardly declare its own regulations invalid, but could very well amend its regulations to correct any shortcomings in how its regulations interpreted a statute. *Newco* stands for the proposition that a court could reverse a decision of the OTA, but it does not preclude the OTA from determining that an Agency regulation was invalid because it conflicts with a provision of the Revenue and Taxation Code or another regulation.

SVLG was founded in 1977 by one of Silicon Valley's pioneers, David Packard. Today, SVLG serves the innovation economy and its ecosystem by representing hundreds of innovation economy companies of all sizes, the majority of which are technology companies—ranging from software and consumer devices to nanotech, semiconductors, cleantech and biotech. Other SVLG members represent a variety of industries that support the innovation ecosystem, including financial and professional services, healthcare, higher education, nonprofits and more.

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March 20, 2023

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West Sacramento, CA 95798

RE: CalCPA Comments on Office of Tax Appeals March 2023 Interested Parties Meeting Related to Proposed Amendments to the Rules for Tax Appeals

On behalf of the members of the California Society of CPAs (CalCPA), we are providing comments to the Office of Tax Appeals (OTA) March 20, 2023 Interested Parties Meeting related to proposed amendments to the OTA's Rules for Tax Appeals.

CalCPA represents the Certified Public Accountant profession and related professionals working in public accounting firms and businesses throughout California. We work closely with policymakers, tax agencies, standard setters, and other key stakeholders to develop and implement fair, effective and efficient tax policy that streamlines compliance for practitioners, taxpayers, and tax agencies. We also work to provide our members with up-to-date information and guidance on a variety of tax matters.

Established under the Taxpayer Transparency and Fairness Act (AB 102, Chapter 16, Statues of 2017), the OTA serves as an independent pre-payment forum to hear taxpayer appeals from administrative determinations made by the California Department of Tax and Fee Administration related to sales and use taxes and by the Franchise Tax Board relating to income taxes. The stated intent of the Legislature in creating the OTA was to establish an "appeals process that is fair, transparent, consistent, equitable, and impartial." As various OTA provisions and procedures were developed and implemented, CalCPA and other stakeholders worked collaboratively with OTA staff to ensure that, once in practice, the OTA remained aligned with this legislative intent.

Consistent with these efforts, we are providing comments for consideration where we believe proposed OTA regulations may be inconsistent with legislative intent or may benefit from additional clarity. Specifically, our comments address proposed regulations that: (1) would impose conditions on the types of refund claims that can be brought before OTA; (2) limit the issues OTA has jurisdiction to consider; (3) modify the procedures for transitioning appeals originally docketed with the Board of Equalization (BOE); (4) modify the rules of evidence applicable to OTA proceedings; and (5) provide the OTA with unilateral authority to withdraw precedential status for prior opinions,

We offer these comments in the spirit of collaboration with the intention of supporting practical tax policy that supports legislative intent for an "appeals process that is fair, transparent, consistent, equitable, and impartial." Our comments are outlined below in the order that they appear in the current OTA regulations.

1. Proposed Changes to Section 30103: Jurisdiction Over Perfected Refund Claims

Section 30103(a)(4) of the OTA Regulations states the OTA's jurisdiction to hear and decide appeals in cases where the "FTB fails to act on a claim for refund of tax, penalties, fees, or interest within six months after the claim is filed with FTB." In the proposed regulatory changes, the OTA proposes to modify this rule to provide that the jurisdictional grant applies only to "*perfected*" claims for refund, without providing an explanation or definition of that term.

While many refund claims are made through the submission of amended returns, we are concerned that the proposed change could lead to the improper rejection of appeals in cases where claims are made through letters, reasonable cause forms, and other accepted alternatives to amended returns. This is particularly concerning in FTB examinations of complex returns, where there is an accepted practice of submitting letter claims to preserve an issue. We are not aware that the specific format of a refund claim has been a significant issue for OTA appeals. We submit that introducing the undefined concept of a "perfected" claim as a condition for an OTA appeal does not warrant the potential disruption of accepted letter claim practices. Accordingly, we recommend that OTA not adopt this proposed change.

If a change to Section 30103(a)(4) is made to require "perfected" claims, we recommend that the OTA solicit comments on the definition of that term and the process that OTA will follow to determine whether a claim is perfected. Regardless of how it is defined, if the proposed change is adopted we suggest clarifying that it does not divest the OTA of jurisdiction to consider whether, in fact, a claim was perfected if it was rejected by the FTB on that ground. Further, taxpayers should be given the opportunity to present their case at a pre-hearing conference before OTA if an issue is raised by the FTB (or by the OTA) involving the "perfected" nature of a claim.

2. Proposed Changes to Section 30104: Limitations on Jurisdiction

While Section 30103 of the OTA Regulations states the scope of OTA's appeals jurisdiction, Section 30104 narrows that scope by describing various jurisdictional limits. As a threshold matter, we believe that jurisdictional limits for administrative appeals should be avoided since they run counter to the OTA's mission of providing "a fair, objective and timely process for appeals from California taxpayers." When the OTA's jurisdiction is limited, taxpayers are only left with recourse in the courts, which imposes a significant burden and cost on all parties that can be avoided if a dispute can be resolved in the prepayment forum provided for by the OTA.

In the proposed regulations, the OTA proposes to modify the limitations on jurisdiction in Section 30104 to generally preclude consideration of taxpayer challenges to a provision in the California Code of Regulations. Such challenges, which are becoming an increasing feature in tax administration, would be forced into court, effectively denying recourse for taxpayers who

may have legitimate claims, but lack the resources to mount a protracted court proceeding. We believe this limitation is inconsistent with the OTA's role in providing an important check on the broad scope and statewide application of FTB and CDTFA rulemaking authority. In this context, OTA review is important to ensure that potentially inappropriate regulations do not unilaterally control tax and fee policy for the entire state.

The proposed limitation on OTA's jurisdiction to consider regulatory challenges is also inconsistent with the general understanding that OTA (and previously BOE) opinions themselves are the equivalent of regulations – essentially the rules of general application that taxpayers are able to rely on. Retaining jurisdiction to review challenges to regulations and issue opinions resolving those challenges is an important complement to this general rule.

The proposed limitation on OTA jurisdiction is also contrary to prior settled practice before the BOE, a practice that taxpayers and the FTB have long utilized and accepted.[1] That practice allows meritorious challenges to regulations to be resolved short of court review, which advances the interests of fair and efficient tax administration and saves resources for all parties. That practice did not present undue challenges for the BOE should continue before the OTA.

We note that the U.S. Department of Treasury and the Internal Revenue Service (IRS) are currently considering a similar proposal to limit jurisdiction applicable to federal tax disputes heard by the IRS Independent Office of Appeals,[2] which commentators have generally opposed as contrary to effective and efficient tax administration.[3] We echo that same concern in the context of the proposed change to Section 30104, but with a noteworthy difference. The IRS Independent Office of Appeals is not, contrary to its title, truly independent. On the federal level, the independent pre-payment forum for tax disputes is the United States Tax Court. Rather the IRS Independent Office of Appeals is part of the IRS. Its Chief reports to the Commissioner of Internal Revenue and it is advised by attorneys in the IRS Office of Chief Counsel. Accordingly, one can see the argument that the IRS Independent Office of Appeals should generally not be considering challenges to rules or regulations promulgated by the same agency that it is part of. California's OTA, in contrast, is entirely independent of the CDTFA and the FTB and is the functional equivalent of the United States Tax Court in providing a pre-payment forum for resolving tax disputes. Like the Tax Court, which has a robust history of considering, and in many cases, invalidating regulations, OTA should retain jurisdiction to do the same.

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[1] *See Appeal of Standard Oil Company of California*, 1983 WL 15454 (Cal.St.Bd.Eq. March 2, 1983).

[2] Proposed Regulations on Resolution of Federal Tax Controversies by the Independent Office of Appeals, 87 Fed. Reg. 5593 (Sept. 13, 2022).

[3] *See*, *Not so Independent?: New Proposed Rules Constrain IrS's Independent Office of Appeals,* Mayer Brown (Sep. 13, 2022), available at https://www.mayerbrown.com/en/perspectives-events/blogs/2022/09/not-so-independent-new-proposed-rules-constrain-irss-independent-office-of-appeals; Mario Verdolini, Christopher Baratta, *Law Firm Urges IRS to Ditch Proposed Regs on Appeals Referrals,* Tax Notes (Nov. 14, 2022).

Finally, we note that the authorities referenced by the OTA in the proposed regulatory changes does not compel or require the proposed jurisdictional limitations. Consistent with broader jurisdictional limits on the courts, *People ex rel Lynch* v. *Superior Court*, supports the proposition that advisory opinions when there is no actual case or controversy are not permitted.[4] OTA review in cases where regulations have actually been applied by the FTB or CDTFA do not raise these case or controversy concerns. *Newco Leasing Inc. v. State Bd. of Equalization*, involved the BOE's interpretation and application of its own regulations and the court noted that whether those regulations correctly interpret the relevant statutes ultimately rests with the courts. While courts do have ultimate authority over the validity of a regulation, nothing in *Newco Leasing* suggests that intermediate administrative appeals review by OTA is precluded. Therefore, we argue that these cases do not support limiting OTA's jurisdiction.

3. Section 30106: Transitioning Appeals

In connection with the enactment of AB 102, its effective date, and the establishment of the OTA, Section 30106 of the OTA Regulations provides rules for transitioning to the OTA cases pending before the BOE as of January 1, 2018. With the passage of time and that it is unlikely there are any pending cases to which Section 30106 might apply, we recommend that the provision be prospectively removed from regulations to reduce confusion and generally simplify the OTA practice rules.

4. Proposed Changes to Section 30214: Rules of Evidence

Section 30214(f)(5) of the OTA Regulations generally provides that the rules relating to evidence and witnesses contained in the California Evidence Code and the California Code of Civil Procedure do not apply to proceedings before the OTA. In proposed regulatory changes, the OTA modifies this rule to provide that the OTA Panel hearing a case may not make a factual finding on any material disputed fact "based solely on unsworn statements made by a party during the appeal proceeding before OTA, such as statements contained in a party's brief, or arguments made by an unsworn representative during an OTA oral hearing." The proposed change does not define or set any parameters around the definition of a "material disputed fact," nor does it provide any guardrails against parties characterizing an issue as involving a material disputed fact without prior notice. Changes to the OTA Regulations should not be made until these threshold issues are addressed.

The general rule providing that the California Evidence Code does not apply to proceedings before the OTA greatly streamlines proceedings, and reduces costs and burden for all parties, particularly unrepresented taxpayers. The proposed change would materially alter that dynamic and, in our view, is unnecessary. To the extent that the proposed change is driven by a concern over false testimony or representations by a party forming the basis of an OTA decision, that concern is already addressed. For example, in connection with any state investigation (which would include an FTB audit and subsequent appeal to OTA), Section 131 of the California Penal Code makes it a misdemeanor for any person to misrepresent or conceal a material fact. This provision in criminal law provides a sufficient deterrent to taxpayers making false unsworn

[4] 1 Cal.3d 910, 911-912 (1970).

statements to the OTA or including false statements. Further, where taxpayers are represented in proceedings before the OTA, their representatives will generally be subject to various rules of practice, codes of professional conduct, and ethical obligations, which we believe adequately addresses any risk of false statements becoming the basis for an OTA decision.

Finally, to the extent that an issue of material fact is seriously disputed and supported only by unsworn statements, all parties have the ability to request, and the OTA has the ability to unilaterally require, a taxpayer or witness to be put under oath in order to ensure the validity of such statements. Under this scenario, the oath is supported by provisions in the Penal Code governing perjury that, all things considered, does not add significant teeth to the false statement provisions of Section 131 of the Penalty Code, and regardless, are outweighed by the benefits of the general rule that OTA proceedings are not subject to the Evidence Code.[5]

6. Proposed Changes to Section 30503: Withdrawal of Precedential Status of Opinions

In its current form, Section 30503 of the OTA Regulations provides the OTA with the authority to withdraw its *own* opinions previously designated as precedential. This requires that an explanation for the withdrawal be provided. Although not stated in Section 30503, following prior practice of the BOE, that withdrawal can presumably be made prospectively so as not to unduly interfere with settled taxpayer practices and expectations. In the proposed regulations, the OTA expands the scope of Section 30503 to cover prior opinions of the BOE on a subject over which OTA has jurisdiction.

Taxpayers have, over the course of many years, come to rely on a number of opinions from the BOE to help inform their business decisions and taking positions of tax returns.[6] Consistent with that practice, California courts have considered and provided a degree of deference to prior opinions.[7] Providing the OTA with the unilateral authority to withdraw these opinions creates a material risk of disrupting settled practices and expectations on the tax treatment of a number of issues. As noted above, it is also inconsistent with the general understanding that OTA and, previously, BOE opinions are rules of general application that should not be withdrawn without appropriate notice and comment.

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[5] *See*, Section 30214(f) of the OTA Regulations, "Except as otherwise provided … rules relating to evidence and witnesses contained in the California Evidence Code and the California Code of Civil Procedure shall not apply to any proceedings."

[6] *See, e.g.*, Appeal of Monsanto Company, 1970 WL 2471 (Cal.St.Bd.Eq. Nov. 6, 1970) (holding that formula allocation and separate accounting methods can be used to determine if income should be apportioned to the state); Appeal of Merrill, Lynch, Pierce, Fenner & Smith, Inc., 1989 WL 95886 (Cal.St.Bd.Eq. June 2, 1989) (holding that a party relying on Section 25137 of the Code has the burden of proof); Appeal of Stephen D. Bragg, 2003 WL 21403264 (Cal.St.Bd.Eq. May 28, 2003) (holding that a three-factor formula should be applied to income relating to agreements to not-compete and covenant income).

[7] *See, Appeal of Crisa Corporation*, 2002 WL 1400003, *8 (Cal.St.Bd.Eq. June 20, 2022); *Appeal of Bechtel Power Corporation, et al.*, 1997 WL 258471 (Cal.St.Bd.Eq. March 19, 1997); *Appeal of Young's Market Company*, 1986 WL 22859 (Cal.St.Bd.Eq. Nov. 19, 1986); *Appeal of Zenith National Insurance Corp.*, 1998 WL 15204 (Cal.St.Bd.Eq. Jan. 8, 1998).

If the proposed change is adopted, both the current and proposed version of Section 30503 require OTA to explain why precedential status is being withdrawn. That requirement provides helpful transparency, but given the potential effect on settled expectations, a more robust review process—including the opportunity for meaningful public comment—should apply before the precedential status of any opinion from either the BOE or the OTA is withdrawn.

Lastly, we would recommend an additional Interested Parties Meeting to solicit stakeholder review and feedback on any further changes to the OTA's Rules for Tax Appeals. The proposed changes are substantial and complex with significant implications for taxpayers, tax agencies, and tax practitioners. We believe the additional opportunity to review and work with OTA staff to address any outstanding concerns, ensure clarity, and refine language will be well worth the steps to notice an additional Interested Parties Meeting.

We appreciate the consideration of our comments and welcome the opportunity to further discuss these issues with you. Please do not hesitate to contact us should you have any questions.

Sincerely,

Jason Fox
Vice President, Government Relations
California Society of Certified Public Accountants