



STATE OF CALIFORNIA
Taxpayers' Rights Advocate Office MS F385
FRANCHISE TAX BOARD
PO BOX 157
SACRAMENTO CA 95741-0157

02.03.2025

California Taxpayers Association

Dear Bart Baer:

Thank you for submitting your issues for the December 2024 Taxpayers' Bill of Rights Hearing. As the Taxpayers' Rights Advocate, your concerns are important to me.

The following responses are provided by the appropriate program areas within the department:

1. Regulations and Other Guidance

Historically, the FTB has been proactive in offering substantial guidance through regulations and the issuance of Chief Counsel Rulings, Legal Rulings, and other forms of guidance. This support is invaluable for taxpayers as they navigate complex compliance issues and strive to adhere to California's tax laws.

Unfortunately, in the past several years, the FTB has provided very little guidance to the taxpayer community. As an example, the FTB staff describes in its 2025 Rulemaking Calendar document that it has been working on a project to update and amend the "Market Based Sourcing Rules" for almost eight years, with the first Interested Parties Meeting occurring in January 2017 and the latest in July 2020. We acknowledge that the FTB is now moving to adopt these amended regulations formally, but this drawn-out process is an indicator that the regulatory process is not proceeding at an adequate pace.

The issuance of Chief Counsel Rulings has dropped sharply as well. Since 2020, only two CCRs have been issued, compared to 33 in the preceding decade (2011-2020). Many taxpayers have stressed the importance of CCRs and other guidance to clarify uncertain legal areas and mitigate potential penalties. As you are aware, California imposes very severe tax penalties, and taxpayers are very desirous of having the FTB's guidance clear up any gray areas so penalties can be avoided.

Additionally, taxpayers have raised various issues regarding delays from FTB in promulgating regulations. There are currently several outstanding statutes dating back decades that direct FTB to promulgate regulations. Moreover, FTB still has various

regulatory projects that remain outstanding years after interested parties were consulted.

Regulatory guidance is necessary to ensure taxpayers are able to comply with California's complex tax laws. We urge the Board and the FTB leadership to examine the reasons for this slowdown in providing guidance and urge the agency to accelerate its efforts to push forward new regulations without lengthy delays.

Response

We appreciate your concerns regarding FTB's external guidance and the desire for additional guidance. As you noted above, FTB issues external guidance and information in a myriad of ways including FTB Legal Rulings, Chief Counsel Rulings, FTB Notices, and Regulations.

With respect to Chief Counsel Rulings, a taxpayer may request a FTB Legal Ruling from the Legal Division pursuant to the requirements set forth in FTB Notice 2009-08. Over the past couple of years, there has been a sharp decrease in requests for Chief Counsel Rulings overall. In addition, the majority of requests we received over the past couple of years have not pertained to the California income and franchise tax law or did not meet the requirements of FTB Notice 2009-08. However, we continue to work with the taxpayer community on any Chief Counsel Ruling requests we receive.

With respect to regulations, FTB commits to working on our regulatory projects timely and understand the concern regarding the passage of time between interested party meetings and the final promulgation of the regulation. In some instances, the time is due to edits to the regulatory language which necessitates additional public rulemaking notices and to provide the opportunity for the public to respond. In other instances, additional work is required for the agency to perform under the California Administrative Practices Act which may extend the time between the interested party meetings and the final promulgation of the regulation. However, we commit to work on our regulatory projects and to complete the work in a timelier fashion, while ensuring that we do not reduce the time and opportunity the public has to be involved in the rulemaking process.

2. Resolution of Examinations and Tax Controversies

Many taxpayers and representatives have complained about lengthy delays in resolving tax controversies; comments were made at last year's Taxpayers' Bill of Rights hearing about unreasonably long delays in examinations and subsequent controversy procedures. There are many concerns, but we want to highlight three:

First, many taxpayers are concerned that the amount of time to resolve protests is unreasonable and often extends several years. A particular area of irritation is where a protest hearing officer is reassigned to another role in the FTB, a new protest officer is brought in, and much of the proceedings then must go back to the beginning. Historically, the FTB made itself accountable to taxpayers by focusing on the expected

timetable for resolving cases during audits. We recommend that the FTB adopt a similar approach for protests. This could begin with a review to determine the extent of unreasonable delays and seek input from taxpayers, followed by pursuing effective solutions.

Second, many taxpayers have recurring issues, such as apportionment, that are present in multiple tax years, and they unfortunately have to handle the issue in multiple proceedings with different departments of the FTB. It is not uncommon for a taxpayer to confront the same issue during audits, protests, settlements, and even at the Office of Tax Appeals. Recently, the FTB has been resistant to taxpayers' efforts to have these recurring issues resolved on a global scale (for example, by facilitating joint efforts between FTB Audit and Legal to reach a comprehensive resolution). In the past, FTB leadership demonstrated more willingness to work collaboratively with taxpayers to resolve issues globally, including entering into closing agreements coordinated between FTB Audit and Legal, along with issuing a Chief Counsel Ruling for the future treatment of the issue.

Third, the timeline to comply with an information document request for taxpayers and FTB staff is not the same. Taxpayers should be guaranteed a timely response from FTB staff when requesting documents, both to ensure compliance during an audit and for purposes of equity.

We urge the FTB leadership to pursue these approaches to make the administration of the tax law more efficient both for taxpayers and the FTB.

Response

Protests

FTB's Audit Protest Section and Legal Division both resolve protests for assessments that taxpayers believe are incorrect. Our Protest Section is responsible for undocketed protest cases while the Legal Division resolves docketed protest cases. Docketed protest cases generally involve highly complex issues, issues of first impression, and/or large dollar amounts.

FTB historically uses 36 months as a benchmark to determine when protest cases have become "aged." Our goal is to minimize and reduce the number of such protests. During the most recent five fiscal years, we experienced a significant drop in the number of protests more than 36 months old and the number of cases between 24 and 36 months old. Staff continue to work to further reduce the number of such protests. Most protests more than 36 months old are Docketed Protests handled by the Legal Division.

Over the past several years, FTB's Protest Section and Legal Division had many staff retire, depart, or reassigned. As with any organization, loss of experienced staff is both a challenge and an opportunity. As a result, we reassigned cases during the past several years. Unfortunately, this created delays in meeting closure goals on some

docketed protests. With recent hiring efforts and with staff development well underway, we do not expect these staffing challenges to continue long term.

If a taxpayer or representative has concerns regarding the process or timeline on a specific case, we encourage them to reach out to the supervisor or manager so that we can expeditiously address any concern.

Resolution of Recurring Issues

FTB has a number of alternative tools available to resolve disputes other than proceeding through the protest or appeal process. These include Chief Counsel Rulings, Closing Agreements, and Administrative Tax Settlements. Whether FTB will agree to resolve a dispute through one of these processes, including decisions on which process is appropriate, depends on the specific situation.

As noted in FTB Notice 2009-08, FTB will ordinarily not issue a Chief Counsel Ruling where the nature of the case is highly factual. Some examples include whether a unitary business exists, whether a taxpayer is a resident for a particular year, or the value of property as of a certain date. Chief Counsel Rulings are appropriate where there is uncertainty in how the law applies in a particular situation. When FTB staff do not agree with a taxpayer's proposed analysis and conclusions, a ruling is seldom if ever issued. Taxpayer's typically do not request a ruling which they would disagree with.

A Closing Agreement may be an option for a taxpayer who is engaged in our administrative process to resolve specific tax, interest, and/or penalty issues. A Closing Agreement is an agreement as to the proper tax treatment of an issue or transaction and not a settlement agreement of a dispute involving what is or is not the proper tax treatment of an issue or transaction. FTB will not enter into a Closing Agreement for taxable years that are closed by an applicable statute of limitations or for taxable years which have not yet occurred. To the extent your comments seek FTB to enter such agreements, we respectfully decline.

Finally, as noted in FTB Notice 2020-03, FTB is authorized by statute to pursue settlements of civil tax matters in disputes that are the subject of protests, appeals, or refund claims. Requests for settlement are reviewed, and settlements are negotiated by, the staff of the Settlement Bureau. In general, cases must be factually developed and litigating positions established before being considered by the Settlement Bureau staff. FTB is not authorized to settle taxable years which are not the subject of protests, appeals, or refund claims, and thus cannot enter settlement agreements for years which have not occurred.

Timeline

FTB Audit Division staff follow guidelines set forth in Audit Regulations 19032 where we strive to complete an examination within two years. The regulations further set forth guidelines for audit timeliness and communication with taxpayers. The division includes

these guidelines in our Audit Best Practice's communicated and included as part of new auditor training and are further reinforced by Audit management.

A successful resolution of an audit, claim, or protest requires cooperation and a time commitment from both FTB staff and the taxpayer. We include both the supervisor and manager contact information on the initial contact letter if a taxpayer or representative has concerns regarding the process or timeline on a specific case. We encourage taxpayers to reach out to the supervisor or manager to expeditiously address any concerns. In addition, we invite taxpayers to participate in the Audit Customer Experience Survey after completion of an audit or protest. This survey gathers insights and identifies opportunities for a better audit experience for taxpayers. We receive positive feedback and will continue to send surveys to improve accuracy, timeliness, and communication.

3. Utilizing Legal Rulings When Regulations Are More Appropriate

Over the years, the FTB has issued Legal Rulings on various subjects that would be more appropriate for regulations. Recently, the California courts and the Office of Tax Appeals (OTA) invalidated FTB guidance when provided outside of regulations.

For example, the trial court refused to follow the FTB's Technical Advice Memorandum 2022-01, interpreting PL 86-272, because the TAM was not promulgated pursuant to California's Administrative Procedure Act, as seen in the *American Catalog Mailers Association v. Franchise Tax Board* decision issued in December 2023. Additionally, the OTA effectively overturned Legal Ruling 2006-1, indicating that had the FTB formalized its position in a regulation, it might have held differently in the *Appeal of Microsoft*.

CalTax requests that FTB legal staff carefully evaluate when to issue legal rulings vs. when a regulatory process would be more appropriate.

Response

We appreciate CalTax's request regarding this matter. Before FTB issues a Legal Ruling or begins work on a regulatory project, legal staff carefully evaluate and consider a myriad of issues to determine which form of guidance is more appropriate. FTB Legal Rulings and regulations are two very different forms of guidance, each serving a distinct and different purpose. A regulation is any rule, order, or standard of general application adopted by a state agency to implement, interpret, or make specific, any law enforced or administered by that agency. Whereas an FTB Legal Ruling is a legal conclusion by the FTB Chief Counsel, based on existing statutes or/and regulations, about how the existing law, or regulation, should be applied to a specific set of hypothetical facts. Given the purpose of the guidance, FTB will continue to evaluate which form of guidance is most appropriate.

Sincerely,

A handwritten signature in black ink that reads "Angela Jones". The signature is written in a cursive, flowing style.

Angela Jones

Taxpayers' Rights Advocate

cc: Malia M. Cohen

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