Ill-Fated Litigation: Exhausting Administrative Remedies and *De Novo* Review

by Carley A. Roberts and Jessica N. Allen

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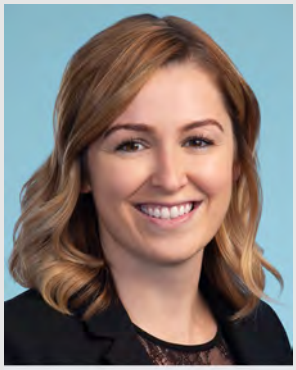

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In the inaugural installment of SeeSALT Digest, Roberts and Allen examine the underpinnings of the exhaustion doctrine and the *de novo* review standard.

I. Introduction

Pre-litigation pitfalls exist at all stages of the state or local tax controversy life cycle. Two principles warrant careful attention; otherwise, mistakes early on can result in a taxpayer not only waiving a valid tax suit for refund but also forfeiting necessary or otherwise valuable evidence. The first principle is the often overlooked and highly jurisdiction-dependent exhaustion of administrative remedies doctrine, which involves determining what levels of administrative challenge are required and how early the grounds on which a taxpayer can bring a suit for refund are established. The second principle is *de novo* review, in which variations among tax types and jurisdictions create critical decision points early in the controversy cycle regarding the evidentiary record should litigation be pursued down the road. While exhaustion of administrative remedies and *de novo* review are separate principles, each can have a significant impact — either separately or together — on the viability of the claim(s) brought in a suit for refund. This article examines the underpinnings of the exhaustion doctrine and the *de novo* review standard and why taxpayers should be aware of their collective importance long before administrative appeals and formal litigation are afoot.

II. Exhaustion of Administrative Remedies

When challenging an assessment or refund claim denial, the available administrative relief procedures and the taxpayer's level of responsiveness during those procedures play an essential role in the success of the taxpayer's challenge. All states, and many local governments, have specific administrative procedures that apply to tax controversies. While exhaustion rules vary from state to state, the general principles supporting the rules are the same.

California, for example, has a well-defined and long-standing judicial exhaustion of administrative remedies doctrine. In 1941 the California Supreme Court held that "where an administrative remedy is provided by statute, relief must be sought from the administrative body, and this remedy exhausted before the courts will act."[1] The failure to exhaust administrative

[1] *Abelleira v. District Court of Appeal*, 17 Cal. 2d 280, 292 (Cal. 1941). The court relied primarily on its understanding of the exhaustion doctrine at the federal level, including citation to many federal cases, in addition to reliance on several cases from other states and six law review articles.

remedies is a limiting factor to the court's jurisdiction to hear a case.[2] The rule acts as a condition precedent, restricting a trial court's ability to find an exception to the rule.[3]

The principle of exhaustion of administrative remedies has two main components. First is the requirement that administrative appeals be brought before the proper tax agency or raised at the proper administrative level before a court considers the taxpayer's cause(s) of action. This issue can arise in class action sales tax cases in which the class seeks to proceed against an individual taxpayer responsible for collecting and remitting a tax rather than seek a refund from the tax agency or vice versa, depending on the jurisdiction.[4] Second, the exhaustion of administrative remedies doctrine requires taxpayers to raise all issues before an administrative body before subsequent judicial review.[5] Because exhausting administrative remedies is a "procedural prerequisite" to an action at law, failure to exhaust each challenge at the administrative level can result in a waiver of a claim in later complaints.[6] Courts are without jurisdiction to consider grounds not set forth in a taxpayer's challenge to an administrative decision.[7] Generally, the administrative level is the taxpayer's opportunity to present all the issues it may want the court to determine in the future,[8] which in turn puts the tax agency on notice of those grounds, satisfying the notice requirement established by the exhaustion doctrine.

A. What Administrative Remedies Must a Taxpayer Exhaust?

Often mistaken to be simple in theory, the exhaustion doctrine can be complicated once put into practice. State and local tax rules can be unclear regarding whether some levels of administrative review are required, as illustrated in the following examples.

First, taxpayers often misinterpret exceptions to the exhaustion doctrine, causing them to skip a necessary administrative step and head straight to court. Incorrectly relying on an exception to the exhaustion doctrine can ultimately result in costly and time-consuming judicial proceedings for the taxpayer and may lead to a taxpayer forfeiting her claim entirely. A California court of appeal in an unpublished decision held that the taxpayers did not exhaust their administrative remedies because they failed to challenge property tax assessments before the local boards of equalization.[9] *In re 2009 Aircraft Tax Refund Cases* involved assessments of personal property taxes by various California counties on commercial aircraft owned by the taxpayers.[10] The taxpayers did not apply for a reduction in the assessments with the respective local boards of equalization.[11] Instead, the taxpayers paid the personal property taxes and filed refund claims with the county boards of equalization to recover the taxes.[12] The refund claims were denied and the taxpayers filed individual suits for refund and declaratory relief actions in a California superior court, which were eventually consolidated. The court dismissed the challenges, holding that the failure to apply for a reduction in the assessments with the local boards of equalization was fatal to the taxpayers' claims.[13]

In an attempt to bypass the first step of the requisite administrative remedies, the taxpayers

[2] *Aronoff v. Franchise Tax Board*, 60 Cal. 2d 177, 180-181 (Cal. 1963) (taxpayer did not exhaust his administrative remedy in which he filed a writ of prohibition against the Franchise Tax Board while a petition for rehearing was pending at the California State Board of Equalization).

[3] However, a California trial court may determine whether a case falls within one of the few exceptions to the exhaustion rule, such as challenges to agency jurisdiction, inadequate administrative remedy, and alternative remedies granted by statute. *See* James E. Reed, "Exhaustion of Remedies," 56 *Calif. L. Rev.* 1061 (1968).

[4] *See, e.g.*, *Loeffler v. Target Corp.*, 58 Cal. 4th 1081 (Cal. 2014); and *Larrieu v. Wal-Mart Stores Inc.*, 872 So. 2d 1157 (La. Ct. App. 2004).

[5] For a further discussion of this issue, see *infra* notes 41-69 and accompanying text.

[6] *Holland v. Union Pacific Railroad Co.*, 154 Cal. App. 4th 940, 946 (Cal. Ct. App. 2007).

[7] *Preston v. State Board of Equalization*, 25 Cal. 4th 197, 205-206 (Cal. 2001) (citing *Atari Inc. v. State Board of Equalization*, 170 Cal. App. 3d 665, 672 (Cal. Ct. App. 1985)).

[8] A limited "futile" exception to the exhaustion doctrine exists when "the administrative agency is not empowered to correct the situation from which judicial relief is sought." *Park 'N Fly of San Francisco v. City of South San Francisco*, 188 Cal. App. 3d 1201, 1208-1209 (Cal. Ct. App. 1987) (citing to *Knoff v. City etc. of San Francisco*, 1 Cal. App. 3d 184, 199 (Cal. Ct. App. 1969)). For example, a taxpayer raising a constitutional challenge may skip administrative action and precede to the courts since an administrative agency lacks jurisdiction to decide a constitutional claim. *Id.*

[9] *See In re 2009 Aircraft Tax Refund Cases*, Cal. Ct. App. (4th App. Dist.) Dkt. No. G053181 (Apr. 13, 2017) (not certified for publication).

[10] *Id.* at *1.

[11] *Id.* at *2.

[12] *Id.*

[13] *Id.* at *3.

relied on an exception to the exhaustion doctrine articulated in *Westinghouse Electric Corp. v. County of Los Angeles*,[14] which relied on the California State Board of Equalization's Assessment Appeals Manual.[15] In *Westinghouse*, the California Court of Appeal stated that the Assessment Appeals Manual allowed a taxpayer challenging a property tax assessment to skip the application to the local board of equalization asking for a reduction in an assessment if "the [property tax] assessment is void for failure to follow statutory procedures."[16] As justification for skipping the first level of administrative review, the *In re 2009 Aircraft Tax Refund Cases* taxpayers argued that the assessments were void under the statutory procedures exception of *Westinghouse* and therefore they exhausted their administrative remedies because they were not required to file an application with the local boards of equalization.[17] The California Court of Appeal disagreed, explaining that an assessor's failure to apply a formula properly, resulting in an incorrect property valuation, does not excuse the requirement that a taxpayer must first apply to a local equalization board.[18] Here, the taxpayers believed that a local board of equalization's incorrect application of a mandatory statutory formula[19] was equivalent to violating a statutory procedure by a local board of equalization and therefore allowed the taxpayers to bypass the exhaustion requirement.[20] However, the Court of Appeal affirmed the trial court's holding that the taxpayers failed to exhaust their administrative remedies, leaving the taxpayers with no further remedy.[21]

Similarly, in a California Supreme Court decision, *Williams & Fickett v. County of Fresno*, the taxpayer attempted to sidestep the application for assessment with the county board of equalization and the county assessment appeals board.[22] While the taxpayer recognized the long-standing principle of exhaustion, it believed the exhaustion principle did not apply to its claim because the assessment was "a nullity as a matter of law."[23] The "nullity as a matter of law" exception is recognized throughout California case law.[24] The California Supreme Court, however, said the use of this exception is "inappropriate in situations where an administrative appeal could eliminate the need for subsequent court proceedings."[25] As a result, the California Supreme Court held that "a claim of nonownership of nonexempt assessed property, by itself, will not provide sufficient basis for invoking the nullity exception and thereby avoiding the assessment appeal process."[26]

Second, taxpayers may jump the gun by initiating administrative proceedings only to later realize they fit into an exception to the exhaustion doctrine. The failure to weigh all options before initiating an administrative proceeding can result in unnecessary steps in the administrative process. An Illinois appellate court in an unpublished opinion prohibited a taxpayer from commencing a judicial proceeding under an exception to the exhaustion doctrine in which the taxpayer already had initiated an administrative proceeding.[27] In response to receiving an estimated assessment of tax from the tax agency, the taxpayer filed a protest and petition for hearing with the Chicago Department of Administrative Hearings.[28] Shortly after filing the protest, the taxpayer realized it fit into an exception to the exhaustion doctrine.[29] The

[14] *Westinghouse Electric Corp. v. County of Los Angeles*, 42 Cal. App. 3d 32 (Cal. Ct. App. 1974).

[15] BOE, "Assessment Appeals Manual" (May 2003, reprinted Jan. 2015).

[16] *Westinghouse Electric Corp.*, 42 Cal. App. 3d at 37 (quoting BOE, "Assessment Appeals Manual," at 109).

[17] *In re 2009 Aircraft Tax Refund Cases*, at *3.

[18] *Id.* The court also noted that "the primary purpose of the exhaustion of administrative remedies doctrine is to afford administrative tribunals the opportunity to decide in a final way matters within their area of expertise before judicial review," a misunderstanding that was also fatal to the taxpayers.

[19] Taxpayers claimed that the assessor failed to properly compute economic obsolescence using a statutorily established formula and therefore the assessments were void. *In Re 2009 Aircraft Tax Refund Cases*, at *1.

[20] *Id.* at *4.

[21] The court of appeal upheld the trial court's decision sustaining the defendants' demurrers without leave to amend on the ground plaintiffs had not exhausted their administrative remedy. *Id.*

[22] *Williams & Fickett v. County of Fresno*, 2 Cal. 5th 1258 (Cal. 2017).

[23] *Id.* at 1, 4.

[24] *Id.* (quoting *Stenocord v. San Francisco*, 2 Cal. 3d 984, 987 (Cal. 1970)).

[25] *Id.* at 10.

[26] *Id.* at 12. The California Supreme Court applied its holding prospectively, explaining that in reaching its decision the court overturned its holding in *Parr-Richmond Industrial Corp. v. Boyd*, 43 Cal. 2d 157 (Cal. 1954), which the taxpayers could have relied on in opting not to pursue timely assessment appeal proceedings. *Id.*

[27] *MagicJack Vocaltec Ltd. v. City of Chicago Department of Finance*, No. 1-17-1015 (Ill. App. 1st. Mar. 21, 2018).

[28] *Id.* at *2.

[29] *Id.* at *3.

exception allowed a taxpayer contesting whether a tax is authorized to skip the administrative process and seek injunctive or declaratory relief in circuit court.[30] The appellate court dismissed the taxpayer's complaint, holding that the exception, while valid, could not be used because the taxpayer had already filed protests with the Department of Administrative Hearings and therefore the taxpayer was required to exhaust its administrative remedies before proceeding to the circuit court.[31]

Third, while not as common, taxpayers should be familiar with the exhaustion doctrine as a defense to unnecessary or premature litigation. In *City of Oakland v. Hotels.com LP*, it was the local tax agency, not the taxpayer, that failed to exhaust its administrative remedies. The U.S. Ninth Circuit Court of Appeals upheld the district court's dismissal because the city of Oakland failed to comply with the ordinance's exhaustion requirement.[32] The local ordinance imposed a hotel tax on some operators in the city, requiring the tax agency to determine and assess the tax, interest, and penalties and provide notice of the assessment to the operator.[33] Before issuing a tax assessment against 10 internet travel companies, Oakland, "jumping the gun," brought suit against the companies "claiming that they failed to calculate and remit occupancy taxes in violation of the [] Ordinance."[34] The city argued that the administrative remedies applied only to the operators, not the taxing agency and that therefore the city was not required to issue an assessment before bringing a suit.[35] The Ninth Circuit rejected the city's argument, explaining that "an action seeking judicial enforcement assumes there is something to enforce."[36] An "assessment and appeal are part of an interrelated administrative process that fixes the tax due."[37]

[30] *Id.*

[31] *Id.* at *4.

[32] *City of Oakland v. Hotels.com LP*, 572 F.3d 958 (9th Cir. 2009).

[33] *Id.* at 960. The operator may appeal the assessment if it disagrees, and the tax administrator must provide a justification for it and conduct a hearing to determine the tax owed. *Id.* The operator may further appeal the hearing determination to the Oakland Taxation and Assessment Board of Review. *Id.*

[34] *Id.* at 959.

[35] *Id.* at 961.

[36] *Id.*

[37] *Id.*

Absent a tax assessment by Oakland, there was nothing for the court to enforce.[38] Thus, the city's appropriate starting point for resolution was the administrative process.[39] The city's failure to exhaust the administrative process was fatal to its claim.[40]

A strong understanding of the exhaustion doctrine is essential to creating a successful case strategy. At the start of a tax controversy — typically at audit — taxpayers need to understand the exhaustion doctrine, its applicable exceptions, and how to apply it. Reassessment is then required at each new level of challenge. Even though a valid exception to the exhaustion doctrine exists, it may be in a taxpayer's favor to proceed through the administrative process first, before filing a court action. But in other situations, it may make more sense to take advantage of an exception, forgo the administrative steps, and immediately file a court action. These decision-making pivot points are highly dependent on the legal issues and facts at play. Misunderstanding the application of the doctrine and its exceptions can be fatal to the taxpayer's claim, as demonstrated in the *In re 2009 Aircraft Tax Refund Cases* decision. Also, as demonstrated in *Hotels.com LP*, it is essential that taxpayers be aware of the exhaustion requirements imposed on the state or local agencies as a defense to an unripe judicial proceeding. Not only does an assessment provide the purported tax due, but it may provide the taxpayer with essential information regarding the tax agency's position, affording the taxpayer valuable insight to help determine whether to challenge the assessment.

B. Preservation of Issues

In a perfect world, all issues (that is, grounds that form the basis for judicial review) would be "clearly" raised at the administrative level. While mistakenly sidestepping a level of administrative review is a more apparent violation of the exhaustion doctrine, oftentimes disputes exist over whether taxpayers properly and adequately stated their causes of action, defenses, or the

[38] *Id.*

[39] *Id.*

[40] *Id.* at 960.

grounds for each issue. Oversight is easy, as far too often taxpayers and tax administrators alike believe they will have a second chance at an appeal challenge to establish the causes of action, defenses, or grounds for the issues that form the basis of a claim.[41]

Preservation of issues in the exhaustion context is tied to the public policy of conserving judicial resources. Before seeking relief in court, a taxpayer is often required to give the tax authority sufficient notice of the taxpayer's claim for refund and its grounds, so that the tax authority is afforded the opportunity to rectify any mistake in tax collection.[42] "Such a rule prevents having an overworked court consider issues and remedies available through administrative channels."[43]

The notion that issues must be preserved at the administrative level is not a new concept. In 2001 the California Supreme Court in *Preston v. State Board of Equalization* stated that a lawsuit must be based "on the grounds set forth in the claim for refund."[44] That is, a taxpayer's claim for refund at the administrative level both "frames and restricts the issues for litigation."[45] Before *Preston*, the California Supreme Court established that the courts do not have jurisdiction to consider grounds not raised in the taxpayer's administrative claim.[46] The pre-litigation pitfalls in this area typically involve confusion over how specific the grounds need to be for a given issue in a refund claim and how to preserve unknown claims that may later surface and become beneficial in framing the overall issues of the case.

The California Supreme Court shed some light on the question of grounds specificity in *Preston*. The taxpayer's transactions at issue in *Preston* involved the transfer of a right to reproduce, but not sell, original artwork. The taxpayer's claim for refund did not specifically raise a copyright issue. Even in the absence of the word "copyright" used at the administrative level, the court held that the unstated contention was "intertwined" and thus implied by the other contentions expressly raised in the taxpayer's claim for refund for purposes of the exhaustion doctrine.[47] In the claim for refund, the taxpayer presented contentions such as "right of reproduction" and "not the sale of original artwork," which were found by the court to sufficiently preserve the taxpayer's reliance on copyright law.[48] The court reasoned that "unstated contentions clearly implied from contentions expressly raised in a claim for refund are sufficiently stated for purposes of exhaustion."[49]

On the other hand, just one month later the California Court of Appeal in *Richard Boyd Industries Inc. v. State Board of Equalization* quickly dispensed with the taxpayer's "intertwined" argument.[50] At the administrative level, the taxpayer claimed that his activity as a construction contractor improving real property limited his sales tax liability regarding some fixtures.[51] Following his administrative challenge, the taxpayer initiated a court action in which he raised a second contention. The taxpayer argued that California law preempted the field of construction contracts.[52] Even though the second contention was not raised at the administrative level, it was regarding the same construction contract and the same fixtures in dispute at the administrative level. Nonetheless, the court, with little explanation, held that the taxpayer could not raise the second contention because it was neither raised in the administrative refund claim nor

[41] In some jurisdictions, a taxpayer might be allowed to raise new issues after the record has been set. For example, the New York State Tax Appeals Tribunal will permit a taxpayer to raise a new legal issue, but not a new factual issue, after the record has been closed at the lower administrative law judge level. *In the Matter of the Petition of Bayerische Beamtenkrankenkasse Ag*, DTA 824762, at *6 (N.Y. Tax App. Trib., Sept. 11, 2017) (citing *In the Matter of the Petition of Jeffrey S. Faupel*, DTA 826255, at *16 (N.Y. Tax App. Trib., Dec. 23, 2015)). New factual claims are precluded as it "deprives the opposing party of the opportunity to offer evidence in opposition of the new factual claim." *In the Matter of the Petition of Faupel*, at *16.

[42] *See, e.g.*, *Preston*, 25 Cal. 4th at 206; *Wertin v. Franchise Tax Board*, 68 Cal. App. 4th 961, 976-977 (Cal. Ct. App. 1998); and *Newman v. Franchise Tax Board*, 208 Cal. App. 3d 972, 980 (Cal. Ct. App 1989).

[43] *See, e.g.*, *Atari Inc.*, 170 Cal. App. 3d at 673.

[44] *Preston*, 25 Cal. 4th at 20 (internal quotations omitted).

[45] *Id.* (internal quotations omitted).

[46] *Atari Inc.*, 170 Cal. App. 3d at 672.

[47] *Id.*

[48] *Id.*

[49] *Id.*

[50] *Richard Boyd Industries Inc. v. State Board of Equalization*, 89 Cal. App. 4th 706 (Cal. Ct. App. 2001).

[51] *Id.* at 713.

[52] *Id.*

intertwined with the contention made in that claim.[53]

Tribunals and courts have construed the grounds set forth in a taxpayer's claim for refund both strictly and liberally, creating a landscape fraught with uncertainty. For example, in *Atari Inc. v. State Board of Equalization*, the California Supreme Court precluded the taxpayer from raising a new claim at the trial court level because of an alleged failure to raise the issue at the administrative level. In its claim for refund, the taxpayer argued that its catalogs were "marketing aids" and therefore its purchases of the catalogs were exempt from sales and use tax under California Code of Regulations section 1670.[54] Later in its trial brief, the taxpayer argued that the catalogs were not marketing aids and therefore section 1670 did not apply, but instead the catalog purchases were not subject to tax because they were sales for resale.[55] The BOE objected, arguing that the scope of the action was limited by the taxpayer's claim for refund and therefore the taxpayer was barred from arguing that the catalogs were exempt from tax as a sale for resale.[56] The California Supreme Court found the taxpayer's claim for refund to be very specific and refused to expand the language to allow the taxpayer to raise any additional claims.[57] In doing so, the court explained that a court may only consider those issues raised in the claim for refund.[58] The court also noted that the rationale behind the rule of confining a complaint (and trial) to issues raised in the claim for refund is part and parcel with the exhaustion of administrative remedies doctrine.[59]

In contrast, the California Court of Appeal allowed a taxpayer to raise equal protection issues for the first time in a court action in *Hibernia Bank*.[60] The BOE argued that the taxpayer was barred from seeking relief under the equal protection clause because the taxpayer failed to raise the issue in any of the documents filed as claims for refund at the administrative level.[61] However, the taxpayer was unaware of the equal protection arguments when the refund claims were filed. The U.S. Supreme Court decided such issues after the taxpayer's claims for refund were filed.[62] As such, the court disagreed with the BOE and held that the taxpayer was allowed to raise the equal protection issues for the first time in court.[63]

In *Delta Air Lines Inc. v. State Board of Equalization*, the California Court of Appeal allowed the taxpayer to challenge the validity of a regulation because the BOE itself put the regulation in issue.[64] The BOE argued that the taxpayer was precluded from challenging the validity of the regulation because of its failure to raise the issue at the administrative level or in superior court.[65] In determining whether the BOE was "adequately apprised" of the issue, the court looked to the administrative hearing and found that the regulation was "the only remedy available" to the taxpayer and the rationale of the administrative decision was based on the defense of the regulation.[66] The BOE also relied on the regulation throughout the litigation to justify its change in audit procedure.[67] The court explained that "there is no rigid requirement that certain precise terms be restated throughout litigation to ensure an issue is not lost."[68] Taking into account the administrative decision and the BOE's reliance on the regulation, the court concluded that the BOE was "adequately apprised" of the issue

[53] *Id.*

[54] *Atari Inc.*, 170 Cal. App. 3d at 671.

[55] *Id.*

[56] *Id.* at 672.

[57] *Id.* at 671.

[58] *Id.* at 673.

[59] *Id.*

[60] *Hibernia Bank v. State Board of Equalization*, 166 Cal. App. 3d 393, 403 (Cal. Ct. App. 1985).

[61] *Id.*

[62] *Id.* The equal protection issues were decided by the U.S. Supreme Court in *Diamond National v. State Equalization Board*, 425 U.S. 268 (1976).

[63] *Id.*

[64] *Delta Air Lines Inc. v. State Board of Equalization*, 214 Cal. App. 3d 518, 529 (Cal. Ct. App. 1989).

[65] *Id.* at 528.

[66] *Id.* at 529.

[67] *Id.*

[68] *Id.*

and therefore the taxpayer's challenge was valid.[69]

III. *De Novo* Review

Of equal importance to the exhaustion doctrine is the principle of *de novo* review. When appealing a final determination from an administrative agency, taxpayers need to apprise themselves of the particular jurisdiction's standard of review. While some state courts and tribunals review the taxpayer's appeal from an administrative decision *de novo*,[70] other states may limit the court's review to the evidentiary record set at the administrative level.[71] When a court reviews a case *de novo*,[72] the court looks at the issues of law and fact as if they have never been ruled on, giving no deference to the administrative agency's final determination.[73]

Taxpayers should carefully consider relying on a *de novo* review process to preserve their right to introduce new evidence after the conclusion of an administrative challenge. Significant variations among jurisdictions have created confusion on exactly when the evidentiary record is established. Taxpayers may find themselves asking: Is the evidentiary record established at the administrative level? If so, at what level? Can a taxpayer introduce new evidence at the next level of appeal? Does failure to provide evidence at the administrative level preclude the taxpayer from later presenting the evidence at the next level of appeal?

During administrative audits, petitions, protests, or other appeals, taxpayers often receive broad information requests from state or local tax agencies asking for "relevant" documentation. The broad scope of the requests can create uncertainty and may result in the taxpayer not providing all or part of the documentation requested. Too often taxpayers are quick to ignore or pay lip service to information and document requests by the tax authority, thinking they will have the opportunity to present the evidence when the dispute reaches a subsequent *de novo* forum. As evidenced by the string of cases below, however, *de novo* does not always mean *de novo*. The interplay between the exhaustion doctrine and the *de novo* principle often results in a trap for the unwary.

Failure to provide evidence at the administrative level can result in the dismissal of the claim or the exclusion of the evidence. California courts have emphasized the importance of presenting both matters of law and fact at the administrative level, before resorting to the courts, ensuring that the agencies are afforded the opportunity to rectify any mistakes.[74] In *E.C. Barnes v. State Board of Equalization*, the taxpayer filed a claim for refund with the BOE. The BOE requested information "essential to support the contentions" in the taxpayer's claim for refund.[75] The taxpayer failed to respond multiple times to the requests, and the BOE denied the taxpayer's claim.[76] The taxpayer's refusal to present the factual documents to the BOE resulted in a failure to exhaust all administrative remedies available, acting as a "jurisdictional bar to court proceedings."[77] The California Court of Appeal affirmed the trial court's summary judgment in favor of the tax authority, holding that the taxpayer's failure to exhaust administrative

[69] In coming to this conclusion, the court relied on the California Supreme Court's decision in *Wallace Berrie & Co.* In *Wallace Berrie*, the BOE argued that the taxpayer failed to challenge the validity of a regulation because the challenge was not articulated in its refund claim. *Wallace Berrie & Co. v. State Board of Equalization*, 40 Cal. 3d 60, 66 fn. 2 (Cal. 1985). The court explained that the taxpayer's assertions in its claim for refund, while not specifically mentioning the regulation, "at least indirectly, launched a substantive attack" on the regulation. *Id.* Furthermore, the court found the BOE's trial stance and failure to raise the "jurisdictional defect" during trial dispelled any question whether the refund claim raised the validity issue. *Id.* The BOE met the taxpayer's validity argument "head on" and proposed an explicit finding, and therefore, while the taxpayer's refund claim could have been more specific, the court found that the BOE was aware of the challenge and that therefore the taxpayer did not fail to exhaust its administrative remedies. *Id.*

[70] *See* D.C. Code section 47-3303; and *Thompson v. King Plow Co.*, 74 Ga. App. 758, 767 (Ga. Ct. App. 1947) (appeals of tax assessments are *de novo* proceedings).

[71] *State Tax Commissioner v. Wilmington Trust Co.*, 266 A.2d 419, 421 (Del. Super. Ct. 1968) (an appeal of an administrative decision to the superior court does not involve a trial *de novo*).

[72] A "hearing *de novo*" is defined by *Black's Law Dictionary* as "giving no deference to a lower court's findings." A "trial *de novo*" is defined by *Black's Law Dictionary* as "a new trial on the entire case . . . conducted as if there had been no trial in the first instance." *Black's Law Dictionary* (2014).

[73] *M&J Leasing Co. v. Executive Director of Department of Revenue of State of Colorado*, 796 P.2d 28, 30 (Colo. App. 1990); and *Gracie LLC v. Idaho State Tax Commissioner*, 237 P.3d 1196, 1198 (Idaho 2010).

[74] *E.C. Barnes v. State Board of Equalization*, 118 Cal. App. 3d 994, 1001 (Cal. Ct. App. 1981).

[75] *Id.* at 997-999 (internal quotations omitted).

[76] *Id.* at 998.

[77] *Id.* at 1002.

remedies left the court with no issues of fact or of law to decide.[78]

In some instances, the evidentiary record could be established as early as the underlying audit. The Wyoming Supreme Court in *Wyoming Department of Revenue v. Qwest Corp.* concluded that evidence not produced to the tax agency during the audit could not be presented later to the court.[79] During audit, the tax agency requested information from the taxpayer, which the taxpayer failed to produce.[80] The taxpayer asked the court to "recognize the difficulty of maintaining voluminous and complex records and to overlook the fact that the taxpayer failed to produce information which existed and was requested" by the tax authority.[81] The court explained that "the burden is on the taxpayer to provide the information necessary" for the tax agency to properly assess the taxpayer's claim.[82] "The [state board of equalization's] role is limited to considering the factual record which was available [] during the assessment process."[83] Allowing a taxpayer to introduce into evidence information not provided at audit, the court explained, would be "denigrat[ing] the entire assessment and audit process."[84]

The California Court of Appeal made a similar holding in *American Chemical Corp. v. County of Los Angeles*.[85] There, the court found that the taxpayer must make a fair and full presentation of evidence to the BOE "as a prerequisite to a judicial attack."[86] The court explained that "were the rule otherwise, the taxpayer could make a perfunctory showing before the board of equalization and reserve his real showing for a subsequent appeal to the courts."[87]

Here, the taxpayer wished to introduce evidence of the BOE's countywide ratio of assessed to market value and evidence offered in the form of testimony in order to prove it was entitled to a reduction of its property tax assessment.[88] Faced with this issue, the court stated that "the issue is the fairness of the administrative hearing and the possibility that evidence not available with reasonable diligence before the administrative agency may be produced on judicial review of the administrative decision."[89] The court held that the evidence was excluded because the taxpayer, with a little diligence, could have produced the evidence at the county board hearing.[90]

IV. Conclusion

Failing to meet pre-litigation prerequisites such as exhausting available administrative remedies may cause a taxpayer to unknowingly waive valid challenges not raised at the administrative level. Also, in some jurisdictions the exhaustion doctrine can preclude the introduction of relevant evidence the taxpayer failed to produce during the administrative appeal process regardless of whether the case is heard *de novo*. In some jurisdictions, the rules can be misleading or nonexistent. All too often taxpayers with valid claims find themselves caught in the failure to exhaust trap. To avoid the trap, taxpayers should carefully vet all issues and evidence as early as possible in the controversy life cycle and continuously along the way. Whether a taxpayer has exhausted any given issue may be more complicated than the record itself reflects. Accordingly, all potential legal arguments and affirmative defenses should be strategically raised — or at a minimum fully considered — at the administrative level, whether at audit or the initial levels of administrative challenge. ■

[78] *Id.*

[79] *See Wyoming Department of Revenue v. Qwest Corp.*, 263 P.3d 622 (Wyo. 2011).

[80] *Id.* at 626.

[81] *Id.*

[82] *Id.* at 629.

[83] *Id.*

[84] *Id.* at 630-631.

[85] *American Chemical Corp. v. County of Los Angeles*, 42 Cal. App. 3d 45, 55 (Cal. Ct. App. 1974). is a property tax appeal from a county board of equalization. In California property tax cases, the factual record is set at the county board level, but the legal record is reviewed *de novo*.

[86] *American Chemical Corp.*, 42 Cal. App. 3d 45, 55.

[87] *Id.* at 54.

[88] *Id.* at 52.

[89] *Id.* at 53.

[90] *Id.* at 54.