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## Memorandum

To: Mr. Vic Anderson  
Supervising Tax Auditor  
Petitions Section (MIC:38)

Date: January 25, 1994

From: John L. Waid  
Tax Counsel

Subject: **Effect of Conditional Endorsements on Payment Checks**

I am responding to your memorandum dated August 30, 1993, to Assistant Chief Counsel Gary J. Jugum. I apologize for the delay in getting back to you.

You indicate that there have been three recent petition cases in which checks were received from the taxpayers which had conditional endorsements on the back and/or were accompanied by correspondence stating that the check was tendered in full satisfaction of the tax obligation and the taxpayer considered the cashing of the check to be a settlement of the dispute. For various reasons, none of these cases qualified for settlement. In two cases, the checks were credited to the liability and the taxpayers notified that such conditional endorsements are not binding on the Board. In the third, after correspondence with the taxpayer in which he reiterated his position that by cashing the check the Board had accepted his final settlement offer, the taxpayer was advised that his compromise offer was not accepted and the payment was refunded. You request our opinion on the propriety of cashing checks from taxpayers with such conditional endorsements on them and if the settlement programs provided by section 7093 and 7093.5 have an impact on this issue.

### OPINION

Under California law the acceptance of a check or draft made out for an amount less than that which is owed and endorsed as being for payment in full discharges the maker's liability and extinguishes his obligation. (Russell v. Riley & Peterson (1927) 82 Cal.App. 728, 732 [256 P. 557].) Such acceptance works an accord and satisfaction. An accord is an agreement by a creditor to accept less than what is owed and a satisfaction is the payment of the lesser amount. (civ. Code §§ 1521, 1523.)

In order for there to be an accord and satisfaction four elements must be present: (1) proper subject matter; (2) competent parties; (3) a consent or meeting of the minds of the parties; and (4) a consideration. (Sierra etc. P. Co. v. Universal Elec. Eng. Co. (1925) 197 Cal. 376, 387 [241 P. 76].) We are of the opinion that this situation grounds out on the very first element. An accord and satisfaction is a remedy to extinguish an obligation based on contract. Although we term an obligation to pay taxes as a "debt," it is not based on contract. "The collection of taxes is not, however, the mere collection of a debt, but is a sovereign act of the state to be exercised as may

be prescribed by the Legislature. ... Although the tax is an obligation from the citizen to the state, it is not of the same character of obligations as exists between citizens, and for the purposes of its collection the state is not limited to the same mode or to the same procedure which it prescribes for individuals in the collection of obligations between themselves.” (People v. Central Pacific R.R. Co. (1895) 105 Cal.576, 588-589 [38 P. 905].)

Thus, a tax obligation does not arise out of a contract. As a result, the amount is fixed by law. While the measure of tax may be the subject of dispute in an audit, the rate cannot be. The state cannot levy more or less and so cannot be implied to have done what the law forbids it to do. (Sierra, supra ..) Therefore, it cannot be implied that the Board agreed to accept a lesser amount as payment of the full amount based on the endorsement on the check.

The state’s power to tax is derived from its sovereign authority, not from any agreement with the taxpayer. (Coast Elevator Co. v. S.B.E. (1975) 44 Cal.App.3d 576, 589 [118 Cal.Rptr. 818].) The general relationship of sovereign and taxpayer does not create any contractual rights. (Southern Service Co., Ltd. v. Los Angeles (1940) 15 Cal.2d 1, 11 [97 P.2d 963]; Cohan v. Alvord (1984) 162 Cal.App.3d 176, 184, fn. 4 [208 Cal.Rptr. 42].) “No element of contract is present here, either implied [citation] or express. [Citation.]” (People v. Union Oil Co. (1957) 48 Cal.2d 476, 481 [310 P.2d 409].) Thus, collection of a tax obligation is not subject to defenses based on the law of contract. (See, Perry v. Washburn (1862) 20 Cal. 318, 350.)

Such remedies as a taxpayer may have must be found in statutes. (Union Oil, supra.) The Legislature provides for settlement of sales and use tax disputes in sections 7093 and (temporarily at least) 7093.5. These statutes do not permit settlement by conditional endorsement on a check. Therefore, such attempt to settle a sales tax case is invalid as not being authorized by statute.

I note, however, that, even if contract law did apply, the way in which these checks were presented prevents them from operating as a settlement offer. Acceptance of a check with a conditional endorsement does not work as an accord and satisfaction if the creditor protests or cashes the check inadvertently or without knowledge of the restriction. (Civ. Code § 1526(a).) Clerks depositing the checks of taxpayers are not vested with authority to make policy decisions. As you note, in the one case where the taxpayer’s assertion of settlement was protested and he reiterated it, the money was refunded.

In sum, then, the relationship of sovereign and taxpayer does not create any contractual rights. Actions to collect taxes are not subject to defenses based on the law of contract. Thus, it cannot be implied that a settlement was made. Such remedies as a taxpayer has must be found in statutes, and those governing settlement of sales and use tax disputes are Sections 7093 and 7093.5. Settlement offers must be made in accordance with and pursuant to those statutes. Therefore, we conclude that the acceptance of a check with a conditional endorsement on the back does not work as a compromise and settlement of a tax dispute. The Board is thus not bound by any such conditional or restrictive endorsement.

On the practical side, however, you can see the problems caused by such endorsements. Management may wish to institute a policy that such checks will not be cashed unless collection

on the account is a problem. I understand, however, that it is a problem with most of these accounts. If the check is to be cashed, our endorsement should be qualified with language such as "under protest" or "accepted as partial payment only." (See Civ. Code § 1526(a).) The account may also qualify under the settlement program.

JLW:es