

**OFFICE OF TAX APPEALS
STATE OF CALIFORNIA**

In the Matter of the Appeal of:) OTA Case No. 18010860
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RONALD McCONNELL) Date Issued: June 8, 2018
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OPINION

Representing the Parties:

For Appellant: Ronald McConnell

For Respondent: Eric R. Brown, Tax Counsel III

For Office of Tax Appeals: Linda Frenklak, Tax Counsel III

A. ROSAS, Administrative Law Judge: Pursuant to California Revenue and Taxation Code section 19045,¹ Ronald McConnell (“Appellant”) appeals an action by the Franchise Tax Board (“FTB” or “Respondent”), determining additional tax of \$3,303, a late-filing penalty of \$825.75, a notice and demand penalty of \$4,447.25, and a filing enforcement fee of \$79, all for the 2014 tax year.

Appellant waived his right to an oral hearing, and therefore the panel decides this matter based on the written record.

ISSUES

1. Did Appellant establish error in Respondent’s determination of additional tax due?
2. Did Appellant establish reasonable cause to abate the late-filing penalty?
3. Did Appellant establish reasonable cause to abate the demand penalty?
4. Did Appellant establish Respondent imposed the filing enforcement fee improperly?

¹ Further statutory references are to the California Revenue and Taxation Code, unless otherwise noted.

FACTUAL FINDINGS

1. During the 2014 tax year at issue, Appellant participated in a real estate sales transaction involving the sale of a condominium in Aliso Viejo, California.² According to a 2014 Real Estate Withholding Tax Statement (Form 593) issued by Regency Real Estate Brokers, Inc., Appellant was identified as the “seller or transferor” of the property in what was described as a “conventional sale or transfer” on November 18, 2014.
2. Appellant did not file a 2014 California return by April 15, 2015.
3. Through its Integrated Non-Filer Compliance (INC) program, Respondent obtained information indicating Appellant received sufficient income in 2014 to require him to file a 2014 California return, including Appellant’s receipt of gross sales proceeds of \$435,000 from the sale of the Aliso Viejo condominium.³
4. On April 20, 2016, Respondent sent Appellant a Demand for Tax Return (Demand), requesting he respond by May 25, 2016, by filing a 2014 return or explaining why a 2014 return was not required.
5. Appellant did not respond to the Demand by the due date.
6. Of relevance to the demand penalty, Appellant also failed to timely file tax returns for tax years 2012 and 2013, which resulted in Respondent taking filing enforcement action against Appellant. For each of the 2012 and 2013 tax years, Respondent issued Appellant a Request for Tax Return and a Notice of Proposed Assessment (NPA).
7. On July 1, 2016, Respondent issued Appellant a NPA for 2014. Based on estimated taxable income of \$222,061, the NPA proposed a tax assessment of \$17,789, minus the real estate withholdings of \$14,486, for a proposed tax deficiency of \$3,303.⁴ The NPA

² At no point during the protest or appeal did Appellant address the details of this real estate sales transaction. Nor did he deny or refute that he sold the Aliso Viejo condominium in 2014.

³ Respondent received a 2014 Real Estate Withholding Tax Statement (FTB Form 593) issued by Regency Real Estate Brokers, Inc., indicating Appellant sold a condominium located in Aliso Viejo, California, on November 18, 2014, and California income tax of \$14,485.50 was withheld from Appellant during escrow. Respondent received information indicating an IRS Form 1099-S was issued to Appellant listing gross proceeds of \$435,000 from the condominium sale. Respondent also learned that an IRS Form 1099-R was issued to Appellant listing a distribution of \$4,518 from United of Omaha Life Insurance Company. In addition, Respondent learned that two IRS Forms 1099-INT were issued to Appellant listing interest paid of \$10 and \$32 from Bank of America.

⁴ The NPA indicated Respondent estimated Appellant’s 2014 income by using one-half of the reported gross proceeds from the sale of California real estate in 2014 (\$217,500), the distribution from United of Omaha Life Insurance Company (\$4,519), and the interest from Bank of America (\$42).

also imposed a late-filing penalty of \$825.75, a notice and demand penalty of \$4,447.25, and a filing enforcement fee of \$79, plus interest.

8. Appellant timely protested the NPA. Respondent replied by letter dated August 24, 2016, granting Appellant until September 22, 2016, to file his 2014 return. Respondent advised Appellant that if he did not file a return by that date, it would issue a Notice of Action (NOA) affirming the NPA.
9. Appellant did not reply to Respondent's letter dated August 24, 2016.
10. On December 8, 2016, Respondent issued a NOA, affirming the NPA.
11. Appellant timely filed this appeal.⁵ At no time during the protest or appeal did Appellant file his 2014 return.

DISCUSSION

Issue 1 - Did Appellant establish error in Respondent's assessment of additional tax?

California residents are taxed upon their entire taxable income, regardless of source. (§17041(a).) Section 18501(a) requires every individual subject to the California Personal Income Tax Law to file a return with FTB specifically stating the items of gross income from all sources and the deductions and credits allowable. Section 19087(a) provides that if a taxpayer fails to file a return, FTB at any time "may make an estimate of the net income, from any available information, and may propose to assess the amount of tax, interest and penalties due."

When FTB makes a tax assessment based on an estimate of income, FTB's initial burden is to show that its assessment is reasonable and rational. (*Appeal of Michael E. Myers*, 2001-SBE-001, May 31, 2001.) When a taxpayer fails to file a valid return and refuses to cooperate in the ascertainment of his or her income, FTB is given "great latitude" in estimating income. (*Appeals of Walter R. Bailey*, 92-SBE-001, Feb. 20, 1992 [estimate based on third-party information reporting]; *Appeal of R. and Sonja J. Tonsberg*, 85-SBE-034, Apr. 9, 1985 [use of third-party information reporting].) "A taxpayer is not in a good position to criticize respondent's estimate of his or her liability when he or she fails to file a required return and, in addition, subsequently refuses to submit information upon request." (*Appeals of Fred R. Dauberger et al.*, 82-SBE-082, Mar. 31, 1982.)

⁵ Appellant mailed his appeal letter to Respondent on December 22, 2016, and Respondent forwarded Appellant's appeal letter to the Office of Tax Appeals (OTA). OTA accepted Appellant's appeal letter as a timely appeal.

Federal courts have held that a taxing agency need only introduce “some evidence” linking the taxpayer with the unreported income. (*Rapp v. Commissioner* (9th Cir. 1985) 774 F.2d 932, 935.) In *Rapp*, the Ninth Circuit Court of Appeals stated, “[o]nce the Government has carried its initial burden of introducing some evidence linking the taxpayer with income-producing activity, the burden shifts to the taxpayer to rebut the presumption by establishing by a preponderance of the evidence that the deficiency determination is arbitrary or erroneous.”⁶ (*Ibid.*, internal citations omitted.) Essentially, after Respondent satisfies its initial burden, its determination is presumed correct and the taxpayer has the burden of proving it wrong. (*Todd v. McColgan* (1949) 89 Cal.App.2d 509.)

Through its INC program, Respondent obtained information linking the taxpayer with income-producing activity. Respondent used this information to estimate Appellant’s income. Based on its income estimate, Respondent made a tax assessment of \$17,789, minus the real estate withholdings of \$14,486, for a proposed tax deficiency of \$3,303. The information obtained through the INC program, including information that Appellant received gross proceeds of \$435,000, provided a minimal factual predicate for Respondent’s assessment.

Appellant failed to establish that Respondent’s determination was arbitrary or erroneous. Although the Demand and the NPA mentioned the real property sale, Appellant has not addressed whether or not he sold California real property in 2014. He has not attempted to show that the real estate sales transaction information was incorrect or erroneous. In addition, he has not shown or attempted to explain whether his taxable gain from the real estate sale may have been less than the amount determined by Respondent.

In the absence of a 2014 return from Appellant and in the absence of adequately supported assertions from Appellant, Appellant is not in a good position to criticize Respondent’s estimate. The information received through its INC program more than adequately supported Respondent’s determination. Despite multiple opportunities to file a 2014 return or otherwise explain why Respondent’s assessment was erroneous, Appellant did neither. Although Appellant stated he was retired and living on his social security income, Appellant did not show that Respondent’s determination was incorrect.

⁶ In *Rapp*, like here, the government had information linking taxpayers with income-producing activities, including a sale of real property.

Therefore, Appellant did not establish error in Respondent's assessment of additional tax.

Issue 2 - Did Appellant establish reasonable cause to abate the late-filing penalty?

Section 19131 provides that Respondent shall impose a late-filing penalty when a taxpayer fails to file a tax return on or before its due date or extended due date unless the taxpayer establishes that the late filing was due to reasonable cause and not willful neglect. Reasonable cause means such cause as would prompt an ordinarily intelligent and prudent businessperson to have so acted under similar circumstances. (*Appeal of Robert T. and M. R. Curry*, 86-SBE-048, Mar. 4, 1986.)

Appellant did not file a 2014 return by the due date of April 15, 2015. Accordingly, Respondent imposed a late-filing penalty in the sum of \$825.75. Appellant does not argue that reasonable cause prevented him from filing his 2014 return by the due date. His sole argument is that his monthly Social Security payments were his only source of income in 2014. However, Appellant fails to address the information showing he received sales proceeds of \$435,000 in 2014 from the sale of California real property. That income generated a filing obligation, and Appellant has not established that his failure to discharge that obligation was due to reasonable cause and not willful neglect. Thus, Appellant is liable for the late-filing penalty.

Issue 3 - Did Appellant establish reasonable cause to abate the demand penalty?

Under Section 19133, Respondent will impose the demand penalty upon a late or unfiled return if the taxpayer fails to respond to a demand for a tax return and Respondent issues a NPA under the authority of Section 19087(a) after the taxpayer failed to timely respond to a demand for a tax return at any time during the four taxable years preceding the year for which the current demand for a tax return is being issued. (Cal. Code Regs., tit. 18, § 19133(b).) The requirement that it be shown that Appellant failed to timely respond to a demand for a return at any time during the four taxable years preceding the year for which the current demand has been issued has been met. For tax years 2012 and 2013, Respondent issued Appellant two requests for a tax return and two NPAs.

When Respondent imposes the demand penalty, the law presumes the penalty was imposed correctly.⁷ (*Appeal of Stephen C. Bieneman*, 82-SBE-148, July 26, 1982.) The penalty

⁷ For the 2014 tax year at issue, Respondent imposed a demand penalty in the sum of \$4,447.25, which is 25 percent of the \$17,789.00 of tax determined.

may be abated if a taxpayer establishes that the failure to respond was due to reasonable cause and not willful neglect. To establish reasonable cause, a taxpayer must show that the failure to respond to a demand occurred despite the exercise of ordinary business care. (*Id.*) The taxpayer's reasons for failing to respond must be such that an ordinarily intelligent and prudent businessperson would have acted similarly under the circumstances. (*Appeal of Howard G. and Mary Tons*, 79-SBE-027, Jan. 9, 1979.) Here, however, there is no allegation or evidence that Appellant's failure to timely respond to the Demand was due to reasonable cause and not willful neglect. Therefore, Appellant has not established reasonable cause to abate the demand penalty.

Issue 4 - Did Appellant establish Respondent imposed the filing enforcement fee improperly?

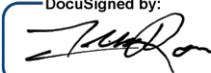
Section 19254(a)(2) requires FTB to impose a filing enforcement cost recovery fee in the event a taxpayer fails to file a return within 25 days after FTB mails a Demand to the taxpayer. Once properly imposed, there is no exception permitting an abatement of this fee. Here, Appellant did not respond to the Demand dated April 20, 2016, within 25 days of FTB mailing the Demand. Thus, Respondent properly imposed a filing enforcement cost recovery fee in the sum of \$79.

HOLDINGS

1. Appellant did not establish error in Respondent's determination of additional tax.
2. Appellant did not establish reasonable cause to abate the late-filing penalty.
3. Appellant did not establish reasonable cause to abate the demand penalty.
4. Appellant did not establish Respondent imposed the filing enforcement fee improperly.

DISPOSITION

Respondent's action is sustained in full.

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Alberto T. Rosas
Administrative Law Judge

We concur:

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Teresa A. Stanley
Administrative Law Judge

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Linda C. Cheng
Administrative Law Judge