OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

In the Matter of the Appeal of:	) OTA Case No. 18011163
	)
JOHN V. BLACK	) Date Issued: August 15, 2018
	)
	)
	)

OPINION

Representing the Parties:

For Appellant:	John V. Black
For Respondent:	Brian Werking, Tax Counsel III
For Office of Tax Appeals:	William J. Stafford, Tax Counsel III

HOSEY, Administrative Law Judge: Pursuant to California Revenue and Taxation Code section 19045,[1] John V. Black (appellant) appeals an action by the Franchise Tax Board (FTB or respondent) on appellant's protest against a proposed assessment in the amount of $746.00 in additional tax, a late-filing penalty of $186.50, a demand penalty of $186.50, and a filing enforcement fee of $78.00, plus applicable interest, for the 2012 tax year.

Appellant waived his right to an oral hearing and therefore the matter is decided on the written record.

ISSUES

1. Whether appellant has established error in the proposed assessment of additional tax.
2. Whether appellant has established that the late-filing penalty should be abated.
3. Whether appellant has established that the demand penalty should be abated.

[1] Unless otherwise indicated, all "Section" references are to sections of the California Revenue and Taxation Code.

4. Whether appellant has established that the filing enforcement cost recovery fee should be abated.

5. Whether a frivolous appeal penalty be imposed and, if so, in what amount.

FACTUAL FINDINGS

1. Appellant has not filed a 2012 California income tax return. Appellant has not filed income tax returns for the 2005, 2006, 2007, 2008, 2009, 2010 and 2011 tax years.

2. Through its Integrated Non-Filer Compliance (INC) Program, FTB obtained computer information reported on a federal Form 1098 from JPMorgan Chase Bank, N.A. (Chase Bank), reporting that appellant paid mortgage interest in 2012 in the amount of $6,122, which indicated income sufficient to trigger the 2012 filing requirement.

3. For the 2012 tax year, FTB estimated appellant's income to be $36,732 by multiplying the amount of reported mortgage interest he paid by six ($6,122 x 6).

4. FTB issued a notice demanding that appellant file a return or explain why no return was required. When appellant neither filed a return, nor supplied information showing that he did not have a filing requirement, FTB issued a Notice of Proposed Assessment (NPA), based on the information received from Chase Bank.

5. Appellant filed a timely protest with FTB, asserting that he did not have a mortgage loan with Chase Bank and, furthermore, that FTB's estimate of his income as being six times the mortgage interest allegedly paid was arbitrary and unreasonable.

6. In response, FTB sent appellant a letter stating that his protest hearing was scheduled for October 14, 2014, at FTB's Santa Ana District Office. In a letter dated October 1, 2014, appellant argued that a member of FTB's audit or legal division was required to conduct the protest hearing. In response, FTB sent appellant a letter, informing appellant of FTB's authority to conduct protest hearings and setting forth the process by which hearings are assigned to various divisions of FTB.

7. Appellant did not appear for the October 14, 2014 protest hearing.

8. Thereafter, FTB affirmed the NPA in a Notice of Action (NOA).

9. Appellant then filed this timely appeal.

10. In his filings in this appeal, appellant (referring to himself in the third person) alleges that "it is his belief that he has not made the amount of income necessary in order to file taxes

in 2012, neither federal nor state." Appellant also alleges that he "has no records for that year."

11. FTB issued Demands for Tax Return to appellant for the 2006, 2007, 2008, 2009, 2010 and 2011 tax years, and when appellant failed to respond, FTB issued NPAs for each of those years.

DISCUSSION

Issue 1 – Whether appellant has established error in the proposed assessment.

Section 17041 imposes a tax "upon the entire taxable income of every resident of this state" and upon the entire taxable income of every nonresident or part-year resident which is derived from sources in this state.[2] Section 18501 requires every individual subject to the Personal Income Tax Law (§ 17001 et seq.) to make and file a return with FTB "stating specifically the items of the individual's gross income from all sources and the deductions and credits allowable . . . ." Section 19087(a) provides:

> If any taxpayer fails to file a return, or files a false or fraudulent return with intent to evade the tax, for any taxable year, the Franchise Tax Board, at any time, may require a return or an amended return under penalties of perjury or 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 proposes a tax assessment based on an estimate of income, FTB's initial burden is to show why its proposed assessment is reasonable and rational. (*Appeal of Myers*, 2001-SBE-001, May 31, 2001.)[3] 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

[2] It appears undisputed that appellant resided in California during the 2012 tax year, and appellant has not argued otherwise.

[3] Pursuant to the Office of Tax Appeals Rules for Tax Appeals, precedential opinions of the State Board of Equalization (BOE) that were adopted prior to January 1, 2018, may be cited as precedential authority to the Office of Tax Appeals unless a panel removes, in whole or in part, the precedential status of the opinion. (Cal. Code Regs., tit. 18, § 30501, subd. (d)(3).) The BOE's precedential decisions may be accessed at http://www.boe.ca.gov/legal/legalopcont.htm.

addition, subsequently refuses to submit information upon request." (*Appeals of Fred R. Dauberger et al.*, 82-SBE-082, Mar. 31, 1982.)

Federal courts have held that the taxing agency need only introduce some evidence linking the taxpayer with the unreported income. (See *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." (*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.) A taxpayer's failure to produce evidence that is within his/her control gives rise to a presumption that such evidence is unfavorable to his/her case. (*Appeal of Cookston*, 83-SBE-048, Jan. 3, 1983.)

FTB's estimation of appellant's income based upon federal Form 1098 information showing that appellant paid mortgage interest for the tax year at issue, in the amount listed above, is both reasonable and rational. (see *Appeal of Bailey*, *supra*; *Appeal of Tonsberg*, *supra*.) Appellant asserts that FTB's proposed assessment is erroneous because he did not have a mortgage loan with Chase Bank in the 2012 tax year and therefore did not make "mortgage interest" payments to Chase Bank. In support, appellant provides various documents from Chase Bank. The documents appear to show that appellant made principal and interest payments to Chase Bank in the 2012 tax year in relation to a home equity line of credit. Appellant contends that "[f]amily, friends, the community and charities have helped support" him. As for how appellant apparently made payments to Chase Bank for the 2012 tax year, appellant asserts: "appellant can only say that it is by the grace of God." We find appellant's statements, without any supporting documentation, do not overcome the presumption of correctness that applies to FTB's deficiency. (*Welch v. Helvering* (1933) 290 U.S. 111, 115.) We note that the courts have rejected unsupported arguments that an individual supported himself with nontaxable sources of income. For example, in *Kindred v. Commissioner*, T.C. Memo. 1979-457, aff'd (6th Cir. 1982) 669 F.2d 400, the taxpayer, a tax protestor, argued that he supported himself with gifts, savings,

and subsistence farming but refused to provide supporting evidence.[4] The court rejected the taxpayer's argument that the IRS had the burden of proof, and found that, because the taxpayer had refused to substantiate his sources of support, the IRS had "great latitude" in estimating the taxpayer's income based on Bureau of Labor statistics. (*Id.*) Like the taxpayer in *Kindred,* appellant asserts that he supported himself with nontaxable sources of income, but refuses to provide supporting evidence. FTB reconstructed the taxpayer's income based on the Form 1098 it received for the tax year at issue. Appellant has not provided a credible explanation as to how he was making the Chase Bank payments or paying for the cost of living during the 2012 tax year. Here, appellant had the burden of proving error in FTB's proposed assessments of additional tax, and he failed to meet that burden of proof.

Appellant argues that FTB's estimate of his income as being six times the mortgage interest paid (as reported on the Form 1098) is arbitrary and not reasonable. FTB states that its use of a ratio of six times the mortgage interest paid is based on "an analysis of tax returns filed by California residents and third-party data (e.g., federal Form 1098 data provided by the Internal Revenue Service) . . .." The evidence of unreported income (information from the Form 1098) has not been contradicted by any credible evidence from appellant. Appellant's assertion that respondent erred in relying on reports from third-party data and calculating his income at six times his interest payments to Chase Bank, standing alone, carries little weight. This is particularly true where, as here, appellant has not filed a return, disputes the accuracy of independent third-party data shown on a Form 1098, and has not provided any credible evidence of his income for any tax year. Here, FTB's use of Form 1098 information from Chase Bank to estimate appellant's taxable income is both reasonable and rational. We hold that the presumption of correctness properly applies to FTB's determination and appellant has not met the burden of demonstrating that FTB's determination is erroneous.

Appellant also argues that FTB failed to provide him with a protest hearing, and failed to give him an opportunity to argue his case. FTB responds that one of its hearing officers scheduled a protest hearing for October 14, 2014, but appellant failed to appear at the scheduled time. Appellant's contention that FTB purported failure to provide appellant with a protest

[4] See also *Shih-Hsieh v. Commissioner*, T.C. Memo. 1986-525 [finding that taxpayer had the burden of showing her sources of income where her expenditures suggested she had some means of support]. The court explained, at page seven of its opinion, that "[i]t is well established that where the taxpayer fails to maintain adequate records, the Commissioner may prove the existence and amount of unreported income by any method that will, in his opinion, clearly reflect the taxpayer's income. [emphasis added]"

hearing opportunity is not borne out by the facts and, in any event, is not a matter over which we have jurisdiction. Our emergency regulations make clear that the Office of Tax Appeals does not have jurisdiction over "[w]hether the appellant is entitled to a remedy for the Franchise Tax Board's actual or alleged violation of any substantive or procedural right, unless the violation affects the adequacy of a notice, the validity of an action from which a timely appeal was made, or the amount at issue in the appeal." (Cal. Code Regs, tit. 18, § 30102(b)(5).) Moreover, in *Bailey, supra,* our predecessor, the Board of Equalization stated that:

> [D]ue process is satisfied with respect to tax matters so long as an opportunity is given to question the validity of a tax at some stage of the proceedings.

Here, FTB's notices to appellant provided him with sufficient notice of the basis for FTB's tax determination and appellant has been provided with an opportunity to question the validity of that determination both before FTB and before this tribunal. To the extent that we have jurisdiction over appellant's claims that FTB's handling of appellant's protest hearing request violated appellant's rights, we find that appellant's claims are utterly without merit.

Issue 2 – Whether appellant has established that the late-filing penalty should be abated.

California imposes a penalty for the failure to file a return on or before the due date, unless it is shown that the failure is due to reasonable cause and not due to willful neglect. (§ 19131.) To establish reasonable cause, a taxpayer "must show that the failure to file timely returns occurred despite the exercise of ordinary business care and prudence, or that cause existed as would prompt an ordinary intelligent and prudent businessman to have so acted under similar circumstances." (*Appeal of Howard G. and Mary Tons*, 79-SBE-027, Jan. 9, 1979.) Illness or other personal difficulties that prevent a taxpayer from filing a timely return may be considered reasonable cause. (See *Appeal of W.L. Bryant,* 83-SBE-180, Aug. 17, 1983.) Appellant offers no evidence of reasonable cause, other than his stated "belief that he has not made the amount of income necessary in order to file taxes in 2012." Appellant has not produced any evidence to show that his purported belief was objectively reasonable. Accordingly, we find no reasonable cause for appellant's failure to file a timely return.

Issue 3 – Whether appellant has established that the notice and demand penalty should be abated.

California imposes a penalty for the failure to file a return or provide information upon FTB's demand to do so, unless reasonable cause prevented the taxpayer from responding to the

request. (§ 19133.) The demand penalty is 25 percent of the total tax, determined without regard to payments and withholding credits. FTB will only impose the demand penalty for an unfiled return if the taxpayer fails to respond to a current Demand for Tax Return and FTB has proposed an assessment under Section 19087(a) after the taxpayer failed to timely respond to a Request for Tax Return or a Demand for Tax Return at any time during the four taxable years preceding the year for which the current Demand for Tax Return has been issued. (Cal. Code Regs., tit. 18, § 19133(b).) The demand penalty is designed to penalize a taxpayer for failing to respond to a notice and demand, not for failing to pay the proper tax. (*Appeal of W. L. Bryant*, 83-SBE-180, Aug. 17, 1983; *Appeal of Frank E. and Lilia Z. Hublou*, 77-SBE-102, July 26, 1977.)

Here, FTB issued Demands for Tax Return to appellant for the 2006, 2007, 2008, 2009, 2010 and 2011 tax years, and when appellant failed to respond, FTB issued a Notice of Proposed Assessment for each of those years. Thus the penalty was properly imposed for the tax year at issue. The burden is on the taxpayer to prove that reasonable cause prevented him from responding to the demand. (*Appeal of Kerry and Cheryl James*, 83-SBE-009, Jan. 3, 1983.) Appellant contends that he had no filing requirement and makes no argument regarding reasonable cause. Accordingly, we find no reasonable cause for appellant's failure to file a return upon FTB's demand.

Issue 4 – Whether appellant has established that the filing enforcement cost recovery fee should be abated.

Section 19254(a)(2) provides that FTB shall impose a filing enforcement cost recovery fee if a person fails or refuses to make and file a tax return within 25 days after a formal legal demand to file the tax return has been mailed to that person by FTB. Appellant does not appear to dispute the amount of the fee, which is set by the Legislature in the annual Budget Act. (§ 19254(b).) FTB has no authority to waive or modify this fee and the taxpayer has not shown that the fee was for any reason invalid or improper. Accordingly, we uphold FTB's imposition of the filing enforcement cost recovery fee.

Issue 5 - Whether a frivolous appeal penalty be imposed and, if so, in what amount.

In accordance with Section 19714, this agency may impose a penalty of up to $5,000 whenever it appears that a proceeding before it has been instituted or maintained primarily for

delay or that the taxpayer's position in the proceeding is frivolous or groundless.[5] Under our regulations, the following non-exclusive list of factors are considered in determining whether to impose the penalty, and in what amount: (1) whether the taxpayer is making arguments that have been previously rejected by the Office of Tax Appeals in a precedential opinion, by the Board in a Formal Opinion, or by the courts; (2) whether the taxpayer is repeating arguments that he advanced unsuccessfully in prior appeals; (3) whether the taxpayer filed the appeal with the intent of delaying legitimate tax proceedings or the legitimate collection of tax owed; and (4) whether the taxpayer has a history of filing frivolous appeals or failing to comply with California's tax laws. (Cal. Code Regs., tit. 18, § 30502(b)(1-4).)[6]

Here, appellant has made similar arguments that have been rejected by the Board. The Board previously imposed a frivolous appeal penalty of $750 for appellant's appeal regarding his 2005 tax year. (*Appeal of John V. Black*, Cal. St. Bd. of Equal. Case No. 449295, Summary Decision adopted Dec. 14, 2010.) Besides the 2012 tax year, FTB issued filing enforcement NPAs against appellant for the 2005-2011 tax years, and those assessments are now final. The record shows that appellant has demonstrated a pattern of filing frivolous appeals and failing to comply with California's tax laws. Appellant was notified of this penalty in the Notice of Action issued by FTB on November 26, 2014. Appellant was notified again when he filed this appeal that if he raised the same frivolous arguments as he has in prior appeals, a penalty of up to $5,000 under Section 19714 could be imposed. Despite this warning, appellant has pursued this appeal raising the same frivolous arguments. We find, therefore, that imposition of a frivolous appeal penalty in the amount of $2,500 is warranted under the circumstances of this case.

HOLDINGS

1. Appellant has failed to demonstrate any error in the proposed assessment of additional tax.
2. Appellant has failed to establish that the late-filing penalty should be abated.
3. Appellant has failed to establish that the notice and demand penalty should be abated.

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[5] Section 19714 refers to the "State Board of Equalization," with regard to the imposition of the frivolous appeal penalty. However, Section 20(b) explains that this phrase now refers to the Office of Tax Appeals because the State Board of Equalization's authority to handle tax appeals has been transferred to this agency.

[6] The Office of Tax Appeals' regulations concerning imposition of the frivolous appeal penalty are virtually identical to its predecessor Board's regulations on this subject. (See Cal. Code Regs., tit. 18, § 5454.)

4. Appellant has failed to establish that the filing enforcement cost recovery fee should be abated.

5. A frivolous appeal penalty in the amount of $2,500 is imposed against appellant pursuant to Section 19714.

DISPOSITION

For the reasons set forth above, FTB's action is sustained in full, and a frivolous appeal penalty of $2,500 is imposed.

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Sara A. Hosey
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Sara A. Hosey
Administrative Law Judge

We concur:

DocuSigned by:
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Linda C. Cheng
Administrative Law Judge

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Douglas Bramhall
Administrative Law Judge