

**OFFICE OF TAX APPEALS
STATE OF CALIFORNIA**

In the Matter of the Appeal of:) OTA Case No. 18011414
)
VICTOR F. PACHECO) Date Issued: June 21, 2018
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OPINION

Representing the Parties:

For Appellant: Tax Appeals Assistance Program (TAAP)¹

For Respondent: Eric A. Yadao, Tax Counsel

For Office of Tax Appeals: Andrew Jacobson, Tax Counsel III

G. THOMPSON, Administrative Law Judge: Pursuant to California Revenue and Taxation Code section 19324,² Victor F. Pacheco (appellant) appeals an action by the Franchise Tax Board (FTB or respondent) denying his claim for refund in the amount of \$999.31³ for the 2014 tax year.

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

ISSUE

Whether appellant has demonstrated reasonable cause for his late payment of tax.

FACTUAL FINDINGS

1. During 2014, appellant earned \$68,450 in wages and received \$84,736 from the sale of stock.

¹ Appellant filed his appeal letter. Earl Cease of the TAAP filed appellant’s reply brief.

² Unless otherwise indicated, all “Section” references are to sections of the California Revenue and Taxation Code.

³ Appellant’s refund claim listed the amount of \$999.31 and sought abatement of the late payment penalty. However, the actual amount of the late payment penalty is \$1,036.63.

2. Appellant did not submit any California income tax payments for the 2014 tax year on or prior to the April 15, 2015 due date, other than income tax withholdings of \$3,163.
3. During 2015, the City and County of San Francisco paid appellant wages of \$51,396. In July of 2015, appellant used part of the proceeds from his sale of stock in 2014 to purchase a condominium in Florida for \$77,300. In August of 2015, appellant quit his job in California and moved to Florida. In Florida, he worked as a substitute teacher, and as a hotel bellman and library assistant. In August of 2015, he withdrew \$33,700.05 from a deferred compensation account, which he used to pay an outstanding Internal Revenue Service (IRS) liability of approximately \$15,465.
4. On or about October 3, 2015, appellant filed a 2014 California resident income tax return (FTB Form 540).⁴ Appellant reported remaining tax due of \$8,293, after taking into account prior withholdings of \$3,163. Appellant submitted \$829.30 as a partial payment and requested an installment payment plan due to economic hardship.
5. Respondent imposed a late payment penalty because appellant did not pay his 2014 tax liability in full by April 15, 2015.
6. Later in 2015, appellant submitted an Offer-in-Compromise (OIC) to FTB. In support of his OIC, appellant provided financial documents, including pay stubs, credit card statements and credit union statements.
 - a. Appellant's financial statements showed that he had approximately \$33,000 in his bank account as of September 2015, which had been reduced to approximately \$13,900 by November 2015.
 - b. Appellant reported that his current monthly net income was \$875 and that his monthly expenses exceeded his net income by \$537.
 - c. Appellant stated he owned a condominium worth \$78,000. He listed \$31,344 of credit card debt, \$15,465 owed to the IRS, and a \$17,000 loan from a friend that he used to purchase the Florida condominium. He indicated that the condominium was not subject to any mortgages.
 - d. Appellant asserted that if he had to pay his 2014 balance due of \$8,306, he would incur extreme economic hardship.

⁴ It appears the return was received or processed by FTB on October 8, 2015.

7. In May of 2016, after reviewing appellant's financial documents, FTB noted that in September 2015, appellant's bank account had a balance in excess of \$33,000.
8. Appellant subsequently withdrew his request for an OIC.
9. On July 20, 2016, appellant paid the total balance due on his 2014 account and filed a claim for refund of the late payment penalty. In his claim for refund, appellant argued that his economic hardship constituted reasonable cause for his late payment of tax.
10. In a letter to appellant dated September 6, 2016, FTB denied appellant's claim for refund.
11. Appellant then filed this timely appeal.

DISCUSSION

FTB's determination is presumed to be correct and a taxpayer has the burden of proving error. (*Appeal of Michael E. Meyers*, 2001-SBE-001, May 31, 2001.)⁵ Unsupported assertions are not sufficient to satisfy a taxpayer's burden of proof. (*Appeal of Aaron and Eloise Magidow*, 82-SBE-274, Nov. 17, 1982.)

Section 19132 subdivision (a)(1)(A) provides that a late payment penalty shall be imposed when a taxpayer fails to timely pay the amount of tax shown as due on the return. The late payment penalty has two parts. The first part is five percent of the unpaid tax. (§ 19132(a)(2)(A).) The second part is a penalty of 0.5 percent of remaining unpaid tax for each additional month, or portion of a month during which the remaining tax is greater than zero.⁶ (§ 19132(a)(2)(B).) The total amount of the penalty may not exceed 25 percent of the total unpaid tax. (§ 19132(a)(3).)

The late payment penalty may be abated if the taxpayer establishes that the failure to make a timely payment of tax was due to reasonable cause and not due to willful neglect. (§ 19132(a)(1).) Reasonable cause exists if it can be shown that the taxpayer acted as an

⁵ Pursuant to the Office of Tax Appeals Rules for Tax Appeals, California Code of Regulations, tit. 18, § 30501(d)(3), 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. BOE's precedential opinions are available for viewing on the BOE's website: <http://www.boe.ca.gov/legal/legalopcont.htm>.

⁶ It appears that FTB's calculation of the late payment penalty did not take into account the \$829.30 payment of tax made by appellant in October of 2015. As a result, it appears the amount of the penalty should be reduced by approximately \$41 (i.e., the product of \$829.30, 0.5% and the 10 months or partial months ending in July of 2016 when appellant paid the remainder of the balance due).

ordinarily intelligent and prudent businessperson would have acted under similar circumstances. (*Appeal of Robert T. Curry and M.R. Curry*, 86-SBE-048, Mar. 4, 1986.)

Undue hardship or inability to pay may constitute reasonable cause “to the extent that the taxpayer has made a satisfactory showing that he exercised ordinary business care and prudence in providing for payment of his tax liability and was nevertheless either unable to pay the tax or would suffer an undue hardship as described in [Treas. Reg. § 1.6161-1(b)] if he paid on the due date.” (Treas. Reg. § 301.6651-1(c)(1).)⁷ A taxpayer’s inability “to pay the tax in spite of the exercise of ordinary business care and prudence in providing for payment of his tax liability” will be determined based on a consideration of “all the facts and circumstances of the taxpayer’s financial situation, including the amount and nature of the taxpayer’s expenditures in light of the income (or other amounts) he could, at the time of such expenditures, reasonably expect to receive prior to the date prescribed for the payment of the tax.” (*Ibid.*) A taxpayer who “made reasonable efforts to conserve sufficient assets in marketable form to satisfy his tax liability and nevertheless was unable to pay all or a portion of the tax when it became due “will be deemed to have exercised ordinary business care and prudence.” (*Ibid.*)

Treasury Regulation section 1.6161-1(b) defines the term “undue hardship.” This regulation requires that the taxpayer show that payment of the tax on the due date would have imposed “undue hardship,” which requires more than merely inconveniencing the taxpayer. “It must appear that substantial financial loss, for example, loss due to the sale of property at a sacrifice price, will result to the taxpayer from making payment on the due date” (Treas. Reg. § 1.6161-1(b).)

As noted above, in order to establish reasonable cause for late payment on the basis of financial difficulties, appellant must show that he exercised ordinary business care and made reasonable efforts to conserve sufficient funds to pay his tax liabilities. Whether payment of the tax would result in undue hardship is determined as of the due date for the tax. Thus, in order for appellant to demonstrate that he had reasonable cause for his late payment of tax, he must show that he made reasonable efforts to conserve sufficient funds to pay the tax by April 15, 2015, but was nevertheless unable to pay the tax by that date without suffering undue hardship.

⁷ Section 19132 is patterned after IRC section 6651. The interpretation and effect given the federal provision by the federal courts and administrative agencies are relevant in determining the proper construction of the California statute. (*Andrews v. Franchise Tax Board* (1969) 275 Cal.App.2d 653, 658.)

The facts here show that appellant has not met this standard. As noted above, he had 2014 income of over \$150,000, including over \$84,000 of income from the sale of stock. An individual exercising ordinary business care would have recognized that tax would be owed in 2015 and taken steps to ensure that he retained sufficient funds to pay the tax that would be owed. There is no evidence that appellant took such steps.

As of April 15, 2015, appellant was gainfully employed, and he was paid \$51,396 by the City and County of San Francisco during 2015. While he did not pay his California income tax by the April 15, 2015 due date, he subsequently quit his job in San Francisco and used part of his savings to purchase a condominium in Florida for \$77,300. There is no indication that, prior to April 15, 2015, appellant sought to estimate his 2014 tax liability and preserve enough savings to pay the tax that would be owed. The evidence that appellant submitted concerning his financial condition after the payment deadline of April 15, 2015, is not relevant because the issue is whether appellant made reasonable efforts, prior to April 15, 2015, to conserve adequate assets to satisfy his 2014 tax liability. Considering all the facts and circumstances, it appears that appellant could have paid the tax owed by April 15, 2015, if he had exercised ordinary business care and diligence.

We note that the IRS waived appellant's federal late payment penalty. However, the IRS did not abate the federal late payment penalty based on a finding of reasonable cause. Instead, it abated the penalty pursuant to an IRS administrative program called First Time Abate in which the IRS abates penalties if a taxpayer has timely filed returns and paid taxes due for the past three years. California law requires a finding of reasonable cause to abate the late payment penalty, and neither the California Legislature nor the FTB have adopted a comparable penalty abatement program.⁸ As a result, the IRS waiver of the penalty does not provide grounds to abate the penalty under California law.

HOLDING

Appellant has not demonstrated reasonable cause for the failure to timely pay tax.

⁸The California Legislature has considered and declined to adopt bills that would change California law to allow a first-time abatement for taxpayers with a history of filing and payment compliance. (See Assem. Bill No. 1777 (2013-2014 Reg. Sess.))

DISPOSITION

FTB's action in denying appellant's claim for refund is modified to allow any refund or credit that results from adjusting the amount of the penalty to reflect appellant's payment of \$829.30 in October 2015 (see footnote 6 of this opinion). FTB's action is otherwise sustained.

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Grant S. Thompson

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Grant S. Thompson

Administrative Law Judge

We concur:

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Michael F. Geary

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Michael F. Geary

Administrative Law Judge

DocuSigned by:

Jeffrey I. Margolis

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Jeffrey I. Margolis

Administrative Law Judge