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OFFICE OF TAX APPEALS
STATE OF CALIFORNIA

In the Matter of the Appeal of:	) OTA Case No. 18010756
	)
	) Date Issued: September 25, 2018
SATVIEW BROADBAND, LTD.	)
	)
	)

OPINION

Representing the Parties:

For Appellants: Tariq Ahmad, President

For Respondent: Eric A. Yadao, Tax Counsel III

M. GEARY, Administrative Law Judge: Pursuant to California Revenue and Taxation Code section 19324,[1] Satview Broadband, Ltd. (appellant) appeals an action by the Franchise Tax Board (FTB) denying appellant's claim for refund of $7,234.18, for the 2009, 2011, 2012, 2013, and 2014 tax years.

Appellant waived its right to an oral hearing. Therefore, we decide the matter based on the written record.

ISSUES

1. Is appellant liable for estimated tax penalties for 2009 and 2011-2014, inclusive?
2. Is appellant liable for late-filing penalties for 2009 and 2011-2014, inclusive?
3. Is appellant liable for penalties for failing to file its 2011 and 2012 returns timely after FTB's demand (demand penalties)?
4. Is appellant liable for penalties for being a nonqualified, suspended, or forfeited entity that was doing business in California and failed to timely file 2011 and 2012 returns after FTB's demand (NQSF penalties)?

[1] Unless otherwise indicated, all statutory ("section" or "§") references are to the Revenue and Taxation Code.

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5. Is appellant liable for filing enforcement cost recovery fees for 2011 and 2012 and a collection cost recovery fee for 2012?
6. Is the Office of Tax Appeals (OTA) authorized to abate or otherwise grant relief from the $250 penalty assessed by FTB for appellant's failure to file its 2009 annual statement with the California Secretary of State?

FACTUAL FINDINGS

1. According to the records of the California Secretary of State:
   a. appellant is a foreign corporation domiciled in Nevada;
   b. on August 22, 2005, appellant registered to conduct business within California;
   c. on January 4, 2010, appellant forfeited its authority to conduct business within California;[2]
   d. on October 15, 2015, appellant's status was "revived" after it paid amounts owed to FTB; and,
   e. on November 24, 2015, appellant voluntarily surrendered its authority to do business within California.
2. According to an Internal Revenue Service Schedule K-1 (Form 1065) issued by Escape Broadband, LLC (Escape) to appellant for the 2012 tax year, appellant was a "Limited partner or other LLC member," and not a "General partner or LLC member-manager" of Escape; appellant's beginning and ending share of profit, loss, and capital was 25 percent; and appellant's share of the loss for 2012 was $885, bringing its ending capital account balance to -$24,055.
3. Appellant failed to timely file its Statement of Information in 2009 with the Secretary of State. The Secretary of State certified the failure to FTB, which assessed a $250 penalty under section 19141 and Corporations Code section 2204, and the Secretary of State has not since decertified appellant's failure to FTB.

[2] We have no evidence regarding the cause for the forfeiture, other than its description on FTB's inter-agency inquiry as an "FTB forfeiture," which usually means the forfeiture was due to a failure to meet tax requirements (file a return, pay taxes).

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4. Appellant concedes it did not file timely California income tax returns for 2009, 2011, 2012, 2013, or 2014, and states that it did not because it was not actively engaged in business in the state during those years.
5. On June 30, 2014, FTB issued to appellant a "Demand for Tax Return" (Demand), which explained that if appellant failed to file a 2012 tax return by July 30, 2014, FTB would assess at least a minimum tax and impose a $200 demand penalty and a cost recovery fee. The Demand also stated that if appellant was a forfeited foreign corporation doing business in California and failed to file a tax return within 60 days after the demand, FTB would impose an additional $2,000 penalty.
6. On August 29, 2014, FTB issued to appellant another Demand, which explained that if appellant failed to file a 2011 tax return by October 1, 2014, FTB would assess at least a minimum tax and impose a $200 demand penalty and a cost recovery fee. The Demand also stated that if appellant was a forfeited foreign corporation doing business in California and failed to file a tax return within 60 days after the demand, FTB would impose an additional $2,000 penalty.
7. On August 29, 2014, FTB issued to appellant a "Notice of Proposed Assessment" (NPA) for 2012 of $3,340.69, consisting of an $800 tax, a $200 demand penalty, a $200 delinquent penalty, a $2,000 NQSF penalty, and a $96 filing enforcement cost recovery fee, plus interest.
8. By letter dated September 5, 2014, appellant responded to the June 30, 2014 Demand (for the 2012 tax year) by explaining that it had not done business in California for over 10 years, and requesting that FTB stop asking it to file tax returns.
9. On November 18, 2014, FTB issued to appellant a "Determination of Filing Requirement Notice of Proposed Assessment – Final," which informed appellant that it was required to file tax returns and pay at least the minimum tax until it legally dissolved or surrendered its authorization to conduct business in California. The document also stated that if appellant filed a 2012 tax return, FTB would withdraw the NPA, and any penalties, interest, and fees would be recalculated based on what appellant reported on its return.
10. By letter dated November 21, 2014, appellant responded to FTB's November 18, 2014 notice by again explaining that appellant had not done business in California for over 10

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years, and again requesting that FTB stop asking it to file returns and stop demanding that it pay taxes it did not owe.

11. On November 24, 2014, appellant filed with the Secretary of State a "Certificate of Surrender of [Its] Right to Transact Intrastate Business in California" (certificate of surrender).

12. On December 19, 2014, FTB issued to appellant an NPA for 2011 of $3,385.57, consisting of an $800 tax, a $200 demand penalty, a $200 delinquent penalty, a $2,000 NQSF penalty, and a $96 filing enforcement cost recovery fee, plus interest.

13. By letter to FTB dated December 23, 2014, appellant again stated that it had not conducted business in California for over 10 years and, therefore, it was not required to file tax returns in California.

14. FTB issued a "Corporation Past Due Notice" to appellant for its 2012 tax year on February 6, 2015, advising appellant of the balance owed for that year and that failure to pay the amount by February 21, 2015, may result in collection fees.

15. FTB issued a Corporation Final Notice Before Levy to appellant for 2012 on March 13, 2015, advising appellant of the balance owed for that year and that failure to pay the amount by March 28, 2015, may result in imposition of a $310 collection fee.

16. On June 2, 2015, appellant filed its California corporate tax returns for 2011, 2012, 2013, and 2014. On August 13, 2015, appellant filed its return for 2009.

17. From June 15, 2015, through December 15, 2015, appellant paid all taxes, interest, penalties, and fees due for the years at issue.

18. On October 13, 2015, FTB received from appellant an "Application for Certificate of Revivor – Corporation" and a "Reasonable Cause – Business Entity Claim for Refund," (claim) for $7,234.18, both dated September 30, 2015. The claim covers all the years at issue. In the claim, appellant stated it failed to file tax returns when it transferred the business to a third party, and FTB did not inform appellant that it must file returns. Appellant also asserted that illness prevented appellant's president from filing the 2009 tax return, that it timely stated its position (that it owed no taxes and was not required to file tax returns) each time FTB sent appellant a notice, and that FTB assessed penalties totaling $7,234.18 for doing business in California without authority when, in fact, appellant did no business in California during the years at issue.

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19. On March 13, 2017, FTB denied the claim in its entirety. This timely appeal followed.

DISCUSSION

Issue 1 - Is appellant liable for estimated tax penalties for 2009 and 2011-2014, inclusive?

As relevant here, every foreign corporation that is qualified to transact intrastate business in California pursuant to chapter 21 of Division 1 of Title 1 of the Corporations Code is subject to the minimum franchise tax ($800) from the date of its qualification until the date it ceases to do business in this state or the date it files a certificate of surrender, whichever occurs later. (§ 23153, subds. (a), (b)(2), (d)(1).) A corporation subject to the franchise tax imposed by Part 11 of the Revenue and Taxation Code must file a declaration of estimated tax and pay the estimated tax for each year, or part of a year, that it is qualified to do business in this state. (§§ 19023, 19025.) If the amount of estimated tax does not exceed the $800 minimum franchise tax, the entire amount of the estimated tax shall be due and payable on or before the fifteenth day of the fourth month of the taxable year. (§ 19025, subd. (a).) A corporation that underpays its estimated tax is penalized by an addition to tax equal to a specified rate of interest applied to the amount of the underpayment. (§§ 19142, 19144.) A penalty for the underpayment of estimated tax is properly imposed where the taxpayer's installment payments are less than the amounts due at the end of the installment periods. (*Appeal of Bechtel, Inc*., 78-SBE-052, July 26, 1978.)[3] There is no general reasonable cause exception to the estimated tax penalty. (*Appeal of Weaver Equipment Co.*, 80-SBE-048, May 21, 1980.)

Here, the evidence shows that appellant first qualified with the Secretary of State to engage in intrastate business in California on August 22, 2005. Appellant does not argue otherwise. It states that it ceased doing business here years before the first year at issue (2009), but it did not file its certificate of surrender until November 24, 2014. As previously noted, section 23153, subdivision (a), states that a foreign corporation that has qualified to do intrastate business in California remains subject to the minimum franchise tax from the date of its qualification until the date it ceases to do business in this state or the date it files a certificate of surrender of its right to transact intrastate business in California, whichever occurs *later*. Because appellant did not file its certificate of surrender until November 24, 2014, it was

[3] Precedential decisions of the State Board of Equalization, designated by "SBE" in the citation, are available on that board's website at <http://www.boe.ca.gov/legal/legalopcont.htm#boeopinion>.

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required to pay the minimum tax with its estimate of tax due by April 15 of each of the tax years at issue. The estimated tax penalty is presumed to be correct and "[i]t is well settled . . . that relief from the penalty . . . is not available upon a showing of 'extenuating circumstances,' 'reasonable cause' or 'a lack of willful neglect.' " (*Appeal of Weaver Equipment Co.*, *supra*.) Appellant does not argue that FTB incorrectly applied the penalty, and it has made no showing that FTB incorrectly calculated the estimated tax penalty.

Regarding appellant's argument that it should be excused from the penalty because it transferred its business to a third party, we have no evidence before us regarding the alleged transfer of appellant's business and can make no finding in that regard. Regardless of the alleged transfer, appellant did not formally surrender its right to conduct business in California until November 24, 2014, and its tax filing and payment obligations continued until that date. Ignorance of the law does not excuse a failure to file a tax return or pay taxes. (*Appeal of David and Marilee Duff*, 2001-SBE-007, Dec. 20, 2001; *Appeal of Oxford Liquor, Inc.*, 79-SBE-052, Mar. 7, 1979.) Accordingly, we conclude that appellant is liable for the estimated tax penalties as determined by FTB.

Issue 2 - Is appellant liable for late-filing penalties for 2009 and 2011 through 2014, inclusive?

During the years at issue, a corporation was required to file its tax return on or before the 15th day of the third month following the close of the tax year. (§ 18601.) Section 19131 requires FTB to impose a late-filing penalty when a taxpayer fails to file a tax return on or before its due date, unless the taxpayer establishes that the late filing was due to reasonable cause and not due to willful neglect. (§ 19131.) The penalty is five percent of the amount of tax required to be shown on the return for every month or fraction thereof that the return is late, up to a maximum of 25 percent. (§ 19131, subd. (a).)

To establish reasonable cause, the 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 ordinarily intelligent and prudent businessman to have so acted under similar circumstances." (*Appeal of Howard G. and Mary Tons*, 79-SBE-027, Jan. 9, 1979.) 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; *Appeal of James C. and Monablanche A. Walshe*, 75-SBE-073, Oct. 20, 1975.)

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The death or serious illness of a taxpayer or a member of a taxpayer's immediate family may constitute reasonable cause for a failure to file a tax return when due. (*United States v. Boyle* (1985) 469 U.S. 241, 243, fn 1.) However, the death or illness must be sufficiently and continuously disruptive to prevent taxpayer's compliance with the law. (*Matter of Carlson v. United States* (7th Cir. 1997) 126 F.3d 915, 923; see also *Estate of Stuller v. United States* (7th Cir. 2016) 811 F.3d 890 (*Stuller*) [holding that a taxpayer who had suffered through many tragic events in the 15 months before her return was due had not established reasonable cause because the events were not sufficiently severe and continuous to have prevented her from complying with the filing requirements].)[4]

Appellant's president states that he was ill in 2010 during the time the 2009 return was due, but he has not provided sufficient evidence to establish that his illness was such that it prevented him from filing the return. His unsupported assertions are not enough to satisfy the burden of proof. (*Appeal of Aaron and Eloise Magidow*, *supra*.)

Appellant argues it is unfair to impose the penalties when it did not conduct business in California and no one informed appellant that it must file returns for each year (or part of a year) before it formally withdrew from California or dissolved. It appears appellant honestly believed no tax was due. However, the law regarding appellant's obligation to timely file returns is clear and, as stated earlier, ignorance of the law is not reasonable cause for failing to comply. Nor is the taxing agency required to remind taxpayers to comply with their statutory obligation to file returns and pay taxes. Accordingly, we conclude that appellant is liable for the late-filing penalties assessed for 2009 and 2011-2014, inclusive.

<u>Issue 3 - Is appellant liable for demand penalties for failing to file its 2011 and 2012 returns timely after FTB's Demands?</u>

FTB may add a penalty of 25 percent of the amount of tax determined if a taxpayer fails to make and file a tax return after notice and demand by FTB, unless the taxpayer establishes the failure was due to reasonable cause and not willful neglect. (§ 19133.) Here, FTB issued two

[4] In *Stuller,* a January 2003 fire destroyed taxpayer's home and killed her husband. She underwent a subsequent hospitalization for double pneumonia and later suffered from depression. A former employee embezzled from her, and trust and probate records needed to manage her affairs were missing. In addition, taxpayer was generally unfamiliar with business matters because her late husband usually handled them. Nevertheless, the Court noted that appellant could attend to many of her business affairs but, for apparently unexplained reasons, was unable to deliver the few remaining records (bank statements) her accountant required to complete the subject return.

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Demands. The first, issued on June 30, 2014, explained that if appellant failed to file a 2012 tax return by July 30, 2014, FTB would assess at least the minimum tax and impose a $200 demand penalty. The second Demand, for the 2011 tax year, was essentially identical, except that it told appellant FTB would assess the same penalty if appellant failed to file a 2011 tax return by October 1, 2014. Appellant did not file a return for 2011 or 2012 within the time allowed. It also has not provided evidence to establish that its failure was due to reasonable cause and not willful neglect. As with the late-filing penalties, appellant's ignorance of the law is not reasonable cause, and appellant does not point to any other cause. We therefore conclude that appellant is liable for demand penalties for failing to file timely its 2011 and 2012 returns after FTB demanded it do so.

Issue 4 - Is appellant liable for NQSF penalties imposed for the 2011 and 2012 tax years?

Section 19135 requires FTB to impose a penalty of $2,000 per tax year when a foreign corporation whose powers, rights, and privileges have been forfeited is "doing business" in this state (within the meaning of section 23101) and fails to make and file a return within 60 days after FTB sends the taxpayer a notice and demand to file the required tax return, unless the failure to file in response to the notice and demand is due to reasonable cause and not willful neglect. FTB has the initial burden of showing that its action is reasonable and rational, and only then does the burden shift to the taxpayer to prove the assessment is wrong. (*Todd v. McColgan* (1949) 89 Cal.App.2d 509; *Appeal of Michael E. Myers*, 2001-SBE-001, May 31, 2001.) FTB's brief notes (and the record establishes) that appellant failed to make and file required returns within 60 days after FTB sent appellant demands to file the required tax returns, and that appellant's failure to file was not attributable to reasonable cause. However, FTB makes no allegation, and the record does not show any basis upon which it may be concluded, that appellant was doing business in California within the meaning of section 23101 during 2011 and 2012, which is a prerequisite for imposing the NQSF penalty.

Since 2011, California law (section 23101) has contained two alternative bases for finding a taxpayer is doing business in this state. Under subdivision (a) of section 23101, a taxpayer is doing business in California if it is "actively engaging in any transaction for financial or pecuniary gain or profit" here. Under section subdivision (b) of section 23101, effective for tax years beginning on or after January 1, 2011, a taxpayer also will be considered to be doing business in California if: (1) it is organized or commercially domiciled in this state; (2) it has

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sales in this state for the applicable tax year that exceed the lesser of five hundred thousand dollars ($500,000) or 25 percent of the taxpayer's total sales; (3) its real and tangible personal property in California exceed the lesser of fifty thousand dollars ($50,000) or 25 percent of the taxpayer's total real property and tangible personal property; or (4) the compensation it pays to employees in California exceeds the lesser of fifty thousand dollars ($50,000) or 25 percent of total compensation paid.[5] (§ 23101, subd. (b).)

FTB does not allege that appellant exceeded any of the thresholds set forth in subdivision (b) of section 23101, nor does FTB point to any transaction or activity that appellant conducted "for financial or pecuniary gain or profit" in California during 2011 and 2012 within the meaning of subdivision (a). The only conceivable basis in the record before us upon which it could be contended that appellant was actively engaging in transactions for profit in California is the fact that appellant held a non-managing minority member interest in Escape, an LLC that admittedly was doing business in California. However, the doing-business status of a pass-through entity – here an LLC taxable as a partnership – is not automatically attributed to its non-managing minority members where, as here, there is no indication that the non-managing minority member had any power or authority, directly or indirectly, to participate in the LLC's management or operations. (*Swart Enterprises, Inc. v. Franchise Tax Bd.* (2017) 7 Cal.App.5th 497 (*Swart*).)

In *Swart*, the taxpayer (Swart) invested $50,000 in exchange for a 0.2-percent non-managing member interest in an LLC (Cypress) that was doing business in California. FTB contended that Swart was doing business in California in 2010 within the meaning of what is now subdivision (a) of section 23101 simply because Swart held an ownership interest in Cypress. The court in *Swart* rejected FTB's position that Swart's passive holding a minority non-managing interest in Cypress established that Swart was "actively engaging in any transaction for financial or pecuniary gain or profit" during the year at issue. It found that the leading authority, *Golden State Theatre & Realty Corp. v. Johnson* (1943) 21 Cal.2d 493, could not be interpreted so broadly as to warrant characterizing Swart's investment activity as "doing business" in the state. (*Swart*, *supra*, 7 Cal.App.5th, at pp. 503-505.) We draw the same conclusion under the instant facts. To hold otherwise would ignore the important distinction between actively and passively (or inactively) engaging in business transactions. (*Ibid.*)

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[5] After 2011, these dollar threshold amounts are adjusted annually for inflation. (§ 23101, subd. (c)(1).)

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FTB also contended in *Swart* that because Cypress elected to be treated as a partnership for tax purposes, Swart should be treated as a general partner in Cypress. (*Swart*, *supra*, 7 Cal.App.5th at p. 505.) Noting that the activities of a general partnership are attributed to its general partners, FTB argued that Swart can "be imputed with 'doing business' in California because Cypress LLC was doing business in California." (*Ibid.*) The court, however, rejected this argument as well. It found that Swart's passive, non-managing member interest was more like a limited partnership than a general partnership, primarily because Swart had no ability to participate in the management and control of Cypress LLC. (*Id*. at p. 503.) And "[b]ecause the business activities of a partnership cannot be attributed to limited partners, Swart cannot be deemed to be 'doing business' in California solely by virtue of its ownership interest in Cypress LLC." (*Ibid.*, citation omitted.) Thus, the court held that Swart's "passively holding a 0.2-percent ownership interest with no right of control over the business affairs of the LLC, does not constitute 'doing business' in California within the meaning of section 23101." (*Id.* at p. 500.)

FTB makes no argument that the operative facts of this appeal are materially different from those at issue in *Swart*. Although appellant's percentage interest in the in-state pass-through entity at issue here is significantly greater than the percentage interest in *Swart* (25 percent as opposed to 0.2 percent), both are minority interests. Without any allegation – much less any showing – that appellant had any ability or authority, directly or indirectly, to influence or participate in the management or operation of Escape's business, we cannot uphold FTB's position that Escape's doing-business status may be attributable to (i.e., flow through to) appellant. Merely pointing to the fact that appellant held a non-managing minority interest in an LLC that was doing business in this state does not, standing alone, satisfy the requirement that FTB show a rational basis for its determination. Consequently, we conclude that appellant is not liable for the 2011 and 2012 NQSF penalties.

<u>Issue 5 - Is appellant liable for filing enforcement cost recovery fees for 2011 and 2012 and a collection cost recovery fee for 2012?</u>

Section 19254 requires FTB to impose filing enforcement cost recovery fees and collection cost recovery fees when FTB notifies a taxpayer that the continued failure to file a return may result in the imposition of the fees, and the taxpayer fails to pay the amount due. The amounts of these fees are adjusted annually to reflect actual collection and enforcement costs.

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The statute does not allow for abatement of or relief from these fees, even on a showing of reasonable cause. (See *Appeal of Michael E. Myers, supra*.)

Here, the fees appear to have been properly imposed, and appellant has made no specific argument concerning them. We find there is no factual or legal basis for abating or relieving the fees. Consequently, appellant is liable for the filing enforcement cost recovery fees imposed for 2011 and 2012 and the collection cost recovery fee imposed for 2012.

Issue 6 - Is OTA authorized to abate or otherwise grant relief from the $250 penalty assessed by FTB for appellant's failure to file its 2009 annual statement with the California Secretary of State?

Corporations Code section 1502 requires every corporation to file an annual statement containing certain information. Corporations Code section 2204 provides that after fulfilling certain notice requirements, the Secretary of State shall certify to FTB the name of any corporation which fails to file the required statement. Upon certification, FTB is required to assess a penalty of $250 against the corporation. (§ 19141; Corp. Code, § 2204(b).) A penalty assessed under section 19141 is a final assessment due and payable immediately, subject only to the authority of the Secretary of State to waive the penalty if it determines that the corporation's failure to file the annual statement was "excusable because of reasonable cause or unusual circumstances that justify the failure to file." (*Ibid*.)

This penalty is assessed by FTB for the Secretary of State. Only the Secretary of State may abate the penalty. Appellant has cited no authority granting to OTA the authority to abate the penalty, and we are aware of none. Consequently, we conclude that OTA is not authorized to abate or otherwise grant relief from the $250 penalty imposed by FTB pursuant to section 19141.

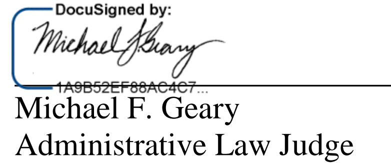
HOLDINGS

1. Appellant is liable for the estimated tax penalty as determined by FTB.
2. Appellant is liable for late-filing penalties for 2009 and 2011-2014, inclusive.
3. Appellant is liable for demand penalties for failing to file timely its 2011 and 2012 returns after FTB demanded it do so.
4. Appellant is not liable for the 2011 and 2012 NQSF penalties.
5. Appellant is liable for the filing enforcement cost recovery fees imposed for 2011 and 2012 and the collection cost recovery fee imposed for 2012.

6. OTA is not authorized to abate or otherwise grant relief from the $250 penalty imposed by FTB pursuant to section 19141.

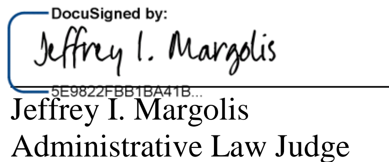
DISPOSITION

We reverse FTB's imposition of the NQSF penalties for 2011 and 2012 and grant refunds of those amounts totaling $4,000 ($2,000 for each year) plus applicable interest; in all other respects, we sustain FTB's denial of the refund claim.

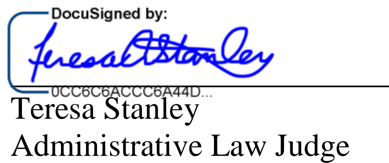


Michael F. Geary
Administrative Law Judge

We concur:



Jeffrey I. Margolis
Administrative Law Judge



Teresa Stanley
Administrative Law Judge