

**OFFICE OF TAX APPEALS
STATE OF CALIFORNIA**

In the Matter of the Appeal of:) OTA Case No. 18011733
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BRENDA L. SHURTLEFF) Date Issued: October 16, 2018
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OPINION

Representing the Parties:

For Appellant: Brenda L. Shurtleff
For Respondent: Eric R. Brown, Tax Counsel III

K. GAST, Administrative Law Judge: Pursuant to California Revenue and Taxation Code section 19324(a),¹ Brenda L. Shurtleff (appellant) appeals an action by the Franchise Tax Board (FTB or respondent) in denying appellant’s claim for refund in the amount of \$4,980.85 for the 2016 tax year.

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

ISSUE

Has appellant established that the late payment penalty imposed under section 19132 should be abated due to reasonable cause and the absence of willful neglect?

FACTUAL FINDINGS

1. Appellant timely filed a 2016 California resident income tax return by the April 18, 2017 due date. On that return, appellant reported taxable 401(k) distribution income from her retirement plan account of \$844,000, as shown on Form 1099-R. Form 1099-R did not

¹ Unless otherwise indicated, all statutory references are to sections of the California Revenue and Taxation Code for the tax year at issue.

- show any California income taxes withheld from the \$844,000 distribution; instead, it only showed that federal income taxes of \$168,800 were withheld from the distribution.
2. After applying a wage withholding credit, appellant's return reported a tax due of \$95,027, which was largely attributable to the 401(k) income. Appellant timely remitted \$10,027 with her return, leaving a balance due of \$85,000 that was not paid with the filing of her return.
 3. On May 15, 2017, appellant untimely remitted the remaining \$85,000 tax due by check.
 4. Subsequently, respondent notified appellant in a Notice of State Income Tax Due that she owed a late payment penalty of \$4,675 and interest of \$305.85, for a total due of \$4,980.85.
 5. Appellant paid the full amount of the late payment penalty, including interest. She then timely filed a claim for refund, contending the penalty should be abated due to reasonable cause and not willful neglect.
 6. By letter dated July 17, 2017, respondent denied appellant's claim for refund. This timely appeal followed.

DISCUSSION

Section 19132 imposes a late payment penalty when a taxpayer fails to pay the amount shown as due on the return on or before the date prescribed for payment of the tax. The late payment penalty has two parts. The first part is 5 percent of the unpaid tax. (§ 19132(a)(2)(A).) The second part is 0.5 percent per month, or a portion of a month, calculated on the outstanding balance. (§ 19132(a)(2)(B).) The aggregate amount of the penalty may not exceed 25 percent of the total unpaid tax. (§ 19132(a)(3).)

The late payment penalty, however, may be abated if the taxpayer can show that the failure to make a timely payment of tax was due to reasonable cause and was not due to willful neglect. (§ 19132(a).) The taxpayer bears the burden of proving both conditions have been met. (*Appeal of Roger W. Sleight*, 83-SBE-244, Oct. 26, 1983.)² To establish "reasonable cause" for the late payment of tax, the taxpayer must show that the failure to timely pay the proper amount of tax occurred despite the exercise of ordinary business care and prudence. (*Ibid.*) Unsupported assertions are not sufficient to satisfy a taxpayer's burden of proof. (*Appeal of Aaron and Eloise*

² Board of Equalization (BOE) opinions are generally available for viewing on the BOE's website: <<http://www.boe.ca.gov/legal/legalopcont.htm#boeopinion>>.

Magidow, 82-SBE-274, Nov. 17, 1982.)

Here, appellant contends her late payment was attributable to reasonable cause and not due to willful neglect. Appellant asserts that at 68 years of age, she wished to purchase and own, for what appears to be the first time in her life, a residential home in 2016, but because she had no established creditworthiness, she was unable to obtain a conventional loan from a bank or other home mortgage lender. Consequently, appellant maintains she had to withdraw a large cash distribution from her 401(k) to fund the purchase price of her newly-acquired home.³ Appellant, however, claims she was unaware she would incur such a sizeable California tax liability on the distribution, and that it was not until her tax preparer informed her, on or about February 28, 2017, of this liability that she filled out a mortgage loan application through a third-party lender for purposes of leveraging the equity in her newly-purchased home to timely pay her taxes. Appellant asserts that the loan process took longer than expected because she still had more documents to complete and information to provide before the funds could be released to her. Therefore, appellant asserts, it was not until May 3, 2017, a few weeks after the April 18, 2017 payment due date of her taxes, that she finally received the funds, a portion of which she promptly used to pay her remaining California tax liability on May 15, 2017.

While appellant's efforts to secure funding to timely pay her 2016 California income tax obligation are commendable, we do not believe she has shown reasonable cause to abate the late payment penalty. Appellant took a large distribution from her 401(k) retirement account for purposes of purchasing her first home. This appears to have been an extraordinary, once-in-a-lifetime financial event for appellant, yet the record contains no evidence indicating she properly planned for it, such as consulting with tax professionals on the tax ramifications of the distribution, as a reasonably prudent businessperson would. Although appellant did promptly pay her California taxes within one month of the due date, the fact remains she was in control of the timing and amount of the 401(k) distribution and therefore had sufficient time to plan for this significant tax event, by setting aside a portion of the distribution for California taxes or by seeking professional tax advice. Appellant did neither.

³ Appellant indicates that out of a total \$844,000 distribution from her 401(k), she used \$675,200 to pay cash for the home. As mentioned above, according to Form 1099-R appellant received, the remaining \$168,800 was withheld by the payor for federal income tax purposes, but nothing was withheld for California income tax purposes. Additionally, appellant does not indicate the exact purchase price of her home and the date when the purchase occurred. However, attached to respondent's brief are public records that appear to show the home was purchased for \$775,000 on or about September 20, 2016, the date the grant deed on the home was recorded.

To be sure, a financial inability to pay taxes when due can rise to the level of reasonable cause and not willful neglect under certain circumstances. (See Treas. Reg. § 301.6651-1(c)(1).)⁴ Here, however, appellant invested all her cash from the 401(k) distribution in a new home without conserving sufficient assets to timely pay her California taxes. Appellant did eventually leverage her home, but because homes are generally illiquid assets—and therefore can take several months to leverage, as it did in this case—appellant should have reasonably foreseen that it would have taken more time than she allotted to accomplish this. Appellant offers no proof that the lender specifically knew of her tax situation and that she needed the loan proceeds at a certain date. There is also no evidence that it was the lender’s own actions she could not control, as opposed to her own, for not closing the loan on time. In short, because appellant did not make reasonable efforts to conserve sufficient liquid assets, or start the loan process early enough, to satisfy her California tax liability, she did not exercise ordinary business care and prudence in attempting to timely pay her taxes.⁵

Finally, appellant maintains that she had the same late payment penalty issue for her 2016 federal income taxes with respect to her inability to timely pay taxes resulting from the 401(k) distribution. She seems to suggest the Internal Revenue Service (IRS) abated the penalty based upon reasonable cause. However, appellant has not submitted any documentary evidence showing the IRS abated the penalty on this basis.

HOLDING

Appellant has not established that the late payment penalty imposed under section 19132 should be abated due to reasonable cause and the absence of willful neglect.

⁴ Although there are no FTB regulations interpreting section 19132, that section is patterned after Internal Revenue Code section 6651. Therefore, the interpretation and effect given the federal provision by the federal courts and administrative bodies are relevant in determining the proper construction of the California statute. (*Andrews v. Franchise Tax Bd.* (1969) 275 Cal.App.2d 653, 658; *Rihn v. Franchise Tax Bd.* (1955) 131 Cal.App.2d 356, 360.) Thus, as relevant here, Treas. Reg. § 301.6651-1(c)(1) provides that “[a] taxpayer will be considered to have exercised ordinary business care and prudence if [s]he made reasonable efforts to conserve sufficient assets in marketable form to satisfy [her] tax liability and nevertheless was unable to pay all or a portion of the tax when it became due.” However, “a taxpayer who invests funds in . . . illiquid assets has not exercised ordinary business care and prudence in providing for the payment of [her] tax liability unless, at the time of the investment, the remainder of the taxpayer’s assets and estimated income will be sufficient to pay h[er] tax or it can be reasonably foreseen that the . . . illiquid investment made by the taxpayer can be utilized (by sale or as security for a loan) to realize sufficient funds to satisfy the tax liability.”

⁵ We, therefore, do not need to address whether there was a lack of willful neglect.

DISPOSITION

Respondent's action in denying appellant's claim for refund is sustained.

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Kenneth Gast
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Kenneth Gast
Administrative Law Judge

We concur:

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Nguyen Dang
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Nguyen Dang
Administrative Law Judge

DocuSigned by:
Amanda Vassigh
7B17E958B7C14AC...
Amanda Vassigh
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