

**OFFICE OF TAX APPEALS  
STATE OF CALIFORNIA**

In the Matter of the Appeal of:  <b>JOSEPH M. KESSEL AND</b>  <b>JOLIE T. KESSEL</b>	) ) ) ) ) )	OTA Case No. 18011217  Date Issued: January 18, 2019
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**OPINION**

Representing the Parties:

For Appellants:	James G. Spradling, CPA
For Respondent:	Samantha Q. Nguyen, Tax Counsel

T. STANLEY Administrative Law Judge: Pursuant to Revenue and Taxation Code section 19324,<sup>1</sup> Joseph M. Kessel and Jolie T. Kessel (appellants) appeal an action by the Franchise Tax Board (FTB or respondent) denying appellants’ claim for refund of \$7,218.05<sup>2</sup> for the 2015 taxable year.

Appellants waived their right to an oral hearing; therefore, the matter is being decided based on the written record.

**ISSUES**

1. Have appellants established reasonable cause to support abatement of the late-payment penalty?
2. Have appellants established that the underpayment of estimated tax penalty should be waived?
3. Have appellants shown that interest may be abated?

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<sup>1</sup> Unless otherwise indicated, all statutory (“section” or “§”) references are to sections of the California Revenue and Taxation Code.

<sup>2</sup> The amount on appeal consists of a refund of a late-payment penalty in the amount of \$4,615.28, an underpayment of estimated tax penalty in the amount of \$1,742.78, and interest in the amount of \$859.99. The total of appellants’ payments and credits indicate that interest was paid in the amount of \$867.73 (after an interest credit of \$.51), which amount is confirmed in respondent’s Exhibit A. Because we sustain respondent’s denial of appellants’ claim for refund, we do not further address that discrepancy.

## FACTUAL FINDINGS

1. On October 10, 2016, appellants timely filed a joint California Resident Income Tax Return (Form 540) for the 2015 taxable year. On their tax return, appellants reported a total tax liability of \$126,650.
2. Appellants claimed income tax withholding of \$2,259 and \$66,700 in estimated tax and other payments, leaving a balance due of \$57,691.
3. Appellants received a K-1 showing pass-through income to appellant-husband from an investment in Canyon Johnson Realty Advisors III LLC (CJRA III), of \$603,757. Appellants contend that 2015 was the first year that appellant-husband received an allocation of income from the passive investment in CJRA III, and that they had previously paid their tax liabilities on time. Shortly after appellants received a final K-1 in September 2016, they filed and paid their additional tax of \$57,691.
4. On October 31, 2016, respondent issued a “Notice of Tax Return Change” and a “Notice of State Income Tax Due,” advising appellants that respondent revised appellants’ balance to add a late-payment penalty, an underpayment of estimated tax penalty, plus interest.
5. Appellants paid the balance due on November 17, 2016.
6. Appellants submitted a Reasonable Cause – Individual and Fiduciary Claim for Refund form on or about November 13, 2016. On November 29, 2016, appellants reiterated, in a letter, their request for an abatement of the penalties and interest, and requested a refund.
7. On January 12, 2017, respondent sent appellants a letter denying appellants’ claim for refund and request for penalty and interest abatement.
8. Appellants timely filed this appeal.

## DISCUSSION

### Issue 1 – Have appellants established reasonable cause to support abatement of the late-payment penalty?

In California, individual income taxpayers must file their return on or before the 15th day of April following the close of the calendar year. (Rev. & Tax. Code, § 18566.) An automatic six-month extension for filing tax returns is granted; however, taxpayers must still pay tax due by the April 15 due date. (Rev. & Tax. Code, § 18567; Cal. Code Regs., tit. 18, § 18567.) Section

19132(a)(1)(A), provides that a late-payment penalty shall be imposed when a taxpayer fails to pay the amount shown as due on the return on or before the original due date of the return. The late-payment penalty has two parts: 1) 5 percent of the total unpaid tax, plus 2) 0.5 percent of the total unpaid tax for every month the payment of tax is late, not to exceed 25 percent of the total unpaid tax. (Rev. & Tax. Code, § 19132.)

The 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 willful neglect. (Rev. & Tax. Code, § 19132(a)(1).) The taxpayer bears the burden to establish reasonable cause. (*Appeal of Sleight*, 83-SBE-244, Oct. 26, 1983.)<sup>3</sup> Reasonable cause requires the taxpayer to show that he or she acted as an ordinarily intelligent and prudent businessperson would have acted under similar circumstances. (*Appeal of Curry*, 86-SBE-048, Mar. 4, 1986.) Unsupported assertions are not sufficient to satisfy a taxpayer's burden of showing a taxpayer exercised ordinary business care and prudence. (*Appeal of Magidow*, 82-SBE-274, Nov. 17, 1982.)

Here, respondent asserts that it properly imposed a late-payment penalty for the 2015 taxable year because appellants did not pay their self-assessed tax liability until October 11, 2016, almost six months after the original due date. Appellants do not dispute that they paid late, but explain that they filed and paid their tax liability as soon as they received a final K-1 from CJRA III in September 2016. Appellants also assert that appellant-husband was not an active participant in CJRA III, and the projected income was "erroneously understated during the year" and through the payment due date in April 2016. Appellants cite their track record for making prompt, quarterly estimated tax payments and argue that this taxable year was the first year that appellant-husband received allocated income from CJRA III. Further, appellants argue that this was the first time they paid late, and they believe it will not happen again.

While we acknowledge that appellants' circumstances may have made it difficult to estimate their income and corresponding tax liability for the 2015 taxable year, it is a well-established rule that delay due to difficulty in obtaining information necessary to complete a return generally will not constitute reasonable cause for purposes of abating the late-payment penalty. (See *Appeal of Campbell*, 85-SBE-112, Oct. 9, 1985 [delay in obtaining records]; *Appeal of Elixir Industries*, 83-SBE-248, Dec. 14, 1983 [late discovery of additional income];

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<sup>3</sup> Precedential opinions of the State Board of Equalization (BOE) are generally available for viewing on the BOE's website: <<http://www.boe.ca.gov/legal/legalopcont.htm#boeopinion>>.

*Appeal of Scott*, 82-SBE-249, Oct. 14, 1982 [lack of necessary information]; and *Appeal of Avco Financial Services, Inc.*, 79-SBE-084, May 9, 1979 [difficulty estimating tax due resulting in late payment penalty].)

There is also no authority which would allow abatement of the late-payment penalty based on appellants' prior good filing or payment history. While the Internal Revenue Service has an administrative program called "First Time Abate" in which it abates timeliness penalties if a taxpayer has timely filed returns and paid taxes due for the past three years, neither the California Legislature nor FTB has adopted a comparable penalty abatement program.<sup>4</sup> We commend appellants for their previous diligence in paying on time; however, under California law, the late-payment penalty may only be abated if the failure to pay on time was due to reasonable cause and not to willful neglect. Appellants have failed to establish the requisite reasonable cause necessary to abate the late-payment penalty.

Issue 2 – Have appellants shown that the underpayment of estimated tax penalty should be abated?

Taxpayers who receive income not subject to sufficient withholding must pay estimated taxes. (Rev. & Tax. Code, § 19136.) Section 19136 conforms, in large part, to Internal Revenue Code (IRC) section 6654, and imposes a mandatory estimated tax penalty for the underpayment of estimated tax payments. Estimated tax payments are generally required of persons who owe more than \$500 in tax, after applying income tax withholdings and credits. (Rev. & Tax. Code, § 19136(c)(2).) IRC section 6654(d) provides for a safe harbor for certain individual taxpayers that relieves them from the estimated tax penalty if their estimated payments total either: 1) 90 percent of the tax shown on the return for the taxable year, or 2) 100 percent of the tax shown on their return for the preceding taxable year. (Rev. and Tax. Code, § 19136(e)(2)(B); IRC, § 6654(d)(1)(B).) However, section 19136.3 modifies that section for taxable years beginning on or after January 1, 2009, in that it removes the option of paying 100 percent of the tax for the preceding taxable year when the adjusted gross income for the taxable year is equal to or greater than \$1 million (in the case of a married couple filing a joint return).

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<sup>4</sup>The 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.))

Neither section 19136 nor IRC section 6654 allow for relief from the underpayment of estimated tax penalty upon a showing of reasonable cause. (*Farhoumand v. Commissioner*, T.C. Memo. 2012-131.) Instead, the law allows respondent to waive the estimated tax penalty only in two circumstances: 1) because of “casualty, disaster, or other unusual circumstances the imposition of such addition to tax would be against equity and good conscience;” or 2) where the failure to timely pay the estimated tax payment was due to reasonable cause, *and* the taxpayer retired after reaching age 62 or the taxpayer became disabled in the taxable year for which the estimated payments were required to be made or in the previous year. (IRC, § 6654(e)(3).)

Appellants argue that unusual circumstances existed because they did not receive the necessary information from CJRA III until September 2016, and that 2015 was the first year they received an allocation of income from CJRA III. However, this type of argument does not provide a valid basis for the abatement of the estimated tax penalty. Accordingly, appellants have not shown that the underpayment of the estimated tax penalty should be abated.

Issue 3 – Have appellants shown that the interest may be abated?

Under section 19001, taxes due must be paid by the original due date of the return, and if not paid by that date, interest must be charged on the balance due from the time of the due date to the date payment was made, pursuant to section 19101. The imposition of interest on a tax deficiency is mandatory once it has been determined that the total tax due was not paid by the due date. (*Appeal of Kubo*, 83-SBE-168, July 28, 1983.) Interest is not a penalty but is compensation for a taxpayer’s use of money that should have been paid to the state. (*Appeal of Yamachi*, 77-SBE-095, June 28, 1977.) There is no reasonable cause exception to the imposition of interest, and interest accrues on the amount assessed as a deficiency regardless of the reason for the assessment. (*Appeal of Goodwin* 97-SBE-003, Mar. 19, 1997.)


Interest may only be abated where authorized by law. To obtain relief from interest, appellants must show that they qualify under the provisions of sections 19104, 19112, or 21012. Appellants’ payment of \$57,691 was credited to their outstanding tax liability on October 11, 2016, almost six months after the original due date. As such, respondent properly imposed interest on the balance due from the original due date of the return to the date payment was made. Appellants neither allege, nor have they proven, that any of the circumstances allowing a waiver of interest apply to them. Thus, abatement of interest is unwarranted.

HOLDINGS


1. Appellants failed to establish reasonable cause to abate the late-payment penalty.
2. Appellants failed to establish a basis to abate the underpayment of estimated tax penalty.
3. Appellants have not shown that interest may be abated.


DISPOSITION

Respondent's denial of appellants' claim for refund is sustained.

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Teresa A. Stanley  
Administrative Law Judge

We concur:

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Tommy Leung  
Administrative Law Judge

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