

OFFICE OF TAX APPEALS
STATE OF CALIFORNIA

In the Matter of the Appeal of:) OTA Case No. 18042767
HUMPHREY MARTINEZ)
) Date Issued: May 6, 2019
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OPINION

Representing the Parties:

For Appellant: Humphrey Martinez
For FTB: David Kowalczyk, Tax Counsel
For Office of Tax Appeals: Josh Lambert, Tax Counsel

D. BRAMHALL, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19045,¹ Humphrey Martinez (appellant) appeals an action by the Franchise Tax Board (FTB) in proposing an assessment of additional tax of \$622, plus interest, for the 2012 tax year.

Appellant failed to request an oral hearing and therefore the matter is being decided based on the written record.

ISSUES

1. Was the Notice of Proposed Assessment (NPA) for tax year 2012 issued within the statute of limitations?
2. Has appellant shown error in FTB’s denial of his refund claim?²
3. Has appellant shown that he is entitled to interest abatement?

¹ Unless otherwise indicated, all “section” or “§” references are to the California Revenue and Taxation Code (R&TC).

² Based upon FTB’s acknowledged misapplication of appellant’s payment of tax and interest assessed, we deem his payment to be a 2012 payment made pending this appeal. Pursuant to R&TC section 19335, as a result of appellant’s payment of the assessed tax and interest, this appeal shall be treated as an appeal from the denial of refund claim.

FACTUAL FINDINGS

1. Appellant timely filed his 2012 California tax return.
2. FTB subsequently received federal information showing that appellant's income included \$24,896 as an early retirement plan distribution and that appellant was assessed a federal 10 percent early distribution tax of \$2,490.
3. Appellant's Wage and Income Transcript shows that Northern Trust issued a Form 1099-R to appellant indicating a gross distribution of \$5,465. Vanguard Fiduciary Trust Company also issued a Form 1099-R to appellant indicating a gross distribution of \$19,430. The Forms 1099-R indicate that they are early distributions.
4. FTB determined that appellant had not reported the corresponding California 2.5 percent early distribution tax. Therefore, on December 4, 2015, FTB issued an NPA and proposed to assess a 2.5 percent early distribution tax of \$622, plus applicable interest.
5. On January 4, 2016, appellant protested the NPA.
6. On February 29, 2016, FTB issued a Notice of State Income Tax Due indicating a balance due of \$678.06.
7. On March 3, 2016, appellant called FTB regarding the Notice of State Income Tax Due and his protest. FTB advised appellant that it may take nine months for FTB to process his protest. Appellant stated that he would make a tax payment while he waited for FTB to process his protest.
8. On March 15, 2016, FTB received appellant's \$678.06 payment but applied the payment to appellant's 2015 account instead of appellant's 2012 account. This resulted in \$259.00 satisfying appellant's tax liability for 2015 and a \$419.06 overpayment, which FTB refunded to appellant on March 22, 2016.
9. Appellant, by letter dated April 3, 2017, advised FTB that it had applied his \$678.06 payment to the wrong tax year.
10. Appellant again, by letter received June 28, 2017, advised FTB that it had applied his \$678.06 tax payment to the wrong tax year.
11. In a letter dated November 1, 2017, FTB conceded it had misapplied appellant's payment of the balance due for 2012 to appellant's 2015 tax year account, presented two options to

correct the error, and offered to abate additional interest back to the date of the original payment.³ Appellant rejected FTB's options by his letter dated November 13, 2017.

12. On December 28, 2017, FTB issued a Notice of Action, affirming the NPA.
13. Appellant filed this timely appeal.

DISCUSSION

1. Was the NPA for the 2012 tax year was issued within the statute of limitations?

In general, FTB must issue a proposed assessment within four years of the date the taxpayer filed his or her California return. (R&TC, § 19057.) Appellant's tax return filed on March 17, 2013, is deemed filed on April 15, 2013, pursuant to R&TC sections 18566 and 19066. FTB issued the NPA on December 4, 2015, which is well within four years of April 15, 2013. Thus, the NPA was timely issued.

2. Has appellant shown error in FTB's proposed assessment/denial of his refund claim?

Internal Revenue Code (IRC) section 72 governs distributions from qualified retirement plans. IRC section 72 imposes a penalty as an additional tax of 10 percent of the amount of the distribution unless the distribution falls within an exception. There are exceptions to the penalty (i.e., additional tax) for early distributions from individual retirement plans under certain circumstances, for example, where the employee is age 59-and-one-half on or after the date the distribution is made or the employee is totally disabled. (IRC, §§ 72(t)(2)(A)(i) and (iii).) R&TC section 17085 conforms to, but modifies, IRC section 72 in relevant part by providing that the federal penalty be computed using a 2.5 percent rate. (R&TC, § 17085(c).)

Appellant did not report a 2.5 percent penalty as additional tax on his 2012 California tax return even though he received \$24,896 in early distributions from qualified retirement plans.

³ FTB's letter acknowledged its error in application of the appellant's payment and stated: "Therefore, we are offering the following to resolve the issue:

1. Send your original payment of \$678.06 within 30 days from the date of this letter. Attach a copy of this letter to your payment to assure proper handling. (On your check or money order, include your account number, the tax year, and the letters 'PA' after the tax year). Interest on this amount will be abated from the date of the date of the original payment.
2. We can move the payment of \$259.00 that was applied to the 2015 tax year to the 2012 tax year. This transfer will create a balance due for the 2015 tax year of \$259.00 plus interest. In this case you will be required to send the \$419.06 that we erroneously refunded.

If your payment is received within 30 days from the date of this notice, no interest will be assessed. However, interest will be assessed on any amount unpaid after 30 days from the date of this notice."

FTB confirmed its determination from appellant's Wage and Income Transcript that shows Northern Trust and Vanguard Fiduciary Trust Company issued Forms 1099-R to appellant, each listing a Distribution Code 1, in the amounts of \$5,465 and \$19,430, respectively. Distribution Code 1 indicates these are early distributions.

Appellant reported the income and withholdings for the distributions on his California tax return but did not report the 2.5 penalty as additional tax. FTB's determination of tax is presumed to be correct, and a taxpayer has the burden of proving error. (*Todd v. McColgan* (1949) 89 Cal.App.2d 509; *Appeal of Quality Tax & Financial Services, Inc.*, 2018-OTA-130P, Oct. 9, 2018; *Appeal of Magidow*, 82-SBE-274, Nov. 17, 1982.) Unsupported assertions are not sufficient to satisfy a taxpayer's burden of proof. (*Appeal of Porreca*, 2018-OTA-095P, Aug. 23, 2018, at p. 4; *Appeal of Magidow, supra.*)

Appellant has not shown that he does not owe the early distribution tax, which was properly assessed pursuant to R&TC section 17085. Appellant does not argue that he qualifies for any exceptions to the tax, only that it was the fault of FTB that the amount was not reported and collected when his return was filed. However, it was appellant's duty to properly report and pay the tax owed when due. As such, appellant has not shown error in the proposed assessment.

3. Has appellant has shown that he is entitled to interest abatement?

Interest is not a penalty but is merely compensation for the taxpayer's use of the money. (R&TC, § 19101(a); *Appeal of Balch*, 2018-OTA-159P, Oct. 9, 2018; *Appeal of Yamachi*, 77-SBE-095, June 28, 1977; *Appeal of Jaegle*, 76-SBE-070, June 22, 1976.) To obtain relief from the imposition of interest, under the facts presented, a taxpayer must qualify per the waiver provisions of R&TC sections 21012, 19112, or 19104. The relief of interest under R&TC section 21012 is not relevant here, as FTB did not provide appellant any written advice. R&TC section 19112 requires a taxpayer to make a showing of extreme financial hardship caused by significant disability or other catastrophic circumstance. However, there is no evidence of these circumstances in the record and, in any event, OTA has no statutory authority to determine whether R&TC section 19112 applies because the waiver of interest pursuant to that section is solely at FTB's discretion.

Under R&TC section 19104(a)(1), FTB may abate all or a part of any interest on a deficiency to the extent that interest is attributable in whole or in part to any unreasonable error or delay committed by FTB in the performance of a ministerial or managerial act. (R&TC,

§ 19104(a)(1).) An error or delay can only be considered when no significant aspect of the error or delay is attributable to the taxpayer and after FTB has contacted the taxpayer in writing with respect to the deficiency or payment. (R&TC, § 19104(b)(1).) There is no reasonable cause exception to the imposition of interest. (*Appeal of Jaegle, supra.*)

In the *Appeal of Kishner*, 99-SBE-007, decided on September 29, 1999, the Board adopted the language from Treasury Regulation section 301.6404-2(b)(2), defining a “ministerial act” as:

[A] procedural or mechanical act that does not involve the exercise of judgment or discretion, and that occurs during the processing of a taxpayer’s case after all prerequisites to the act, such as conferences and review by supervisors, have taken place. A decision concerning the proper application of federal tax law (or other federal or state law) is not a ministerial act.

When a California statute is substantially identical to a federal statute (such as with the interest abatement statute in this case),⁴ OTA may consider federal law interpreting the federal statute as highly persuasive. (*Appeal of Kishner, supra*, (citing *Douglas v. State of California* (1942) 48 Cal.App.2d 835).) In this regard, Treasury Regulation section 301.6404-2(b)(1) defines a “managerial act” as:

[A]n administrative act that occurs during the processing of a taxpayer’s case involving the temporary or permanent loss of records or the exercise of judgment or discretion relating to management of personnel. A decision concerning the proper application of federal tax law (or other federal or state law) is not a managerial act.

A decision concerning the proper application of federal tax law, or other federal or state laws, to the facts and circumstances surrounding a taxpayer’s tax liability is not a ministerial or managerial act. (Treas. Reg., § 301.6404-2(b); *Bucaro v. Commissioner*, T.C. Memo. 2009-247.)

OTA’s jurisdiction in an interest abatement case is limited. We only review FTB’s determination for abuse of discretion. (R&TC, § 19104(b)(2)(B).) To show an abuse of discretion, a taxpayer must establish that, in refusing to abate interest, FTB exercised its discretion arbitrarily, capriciously, or without sound basis in fact or law. (*Woodral v. Commissioner* (1999) 112 T.C. 19, 23.) Interest abatement provisions are not intended to be routinely used to avoid the payment of interest, thus abatement should be ordered only “where

⁴ R&TC sections 19104(a) and (b)(2)(B) are substantially identical to IRC sections 6404 (e) and (h).

failure to abate interest would be widely perceived as grossly unfair.” (*Lee v. Commissioner* (1999) 113 T.C. 145, 149, quoting from H.R.Rep. No. 99-426, at p. 844 (1985), 1986-3 C.B. (Vol.2) 1, 844; Sen.Rep. No. 99-313, at p. 208 (1986), 1986-3 C.B. (Vol.3) 1, 208.)

Appellant argues that FTB was untimely in issuing the NPA. As stated above, the NPA was timely issued, and therefore there was no error or delay regarding the issuance of the NPA. The mere passage of time does not establish error or delay in performing a ministerial or managerial act. (*Lee v. Commissioner, supra*, at p. 150; *Howell v. Commissioner*, T.C. Memo. 2007-204; *Bucaro v. Commissioner, supra*; *Larkin v. Commissioner*, T.C. Memo. 2010-73.) Thus, we find no basis to abate interest on the underpayment of tax noted above.

HOLDINGS

1. Appellant has not shown that the NPA was barred by the statute of limitations.
2. Appellant has not shown error in FTB’s proposed assessment of tax/denial of his refund claim.
3. Appellant has not shown that he is entitled to interest abatement for any interest paid.

DISPOSITION

FTB’s denial of appellant’s refund claim is sustained.

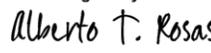
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 Douglas Bramhall
 Administrative Law Judge

We concur:

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 Linda C. Cheng
 Administrative Law Judge

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 Alberto T. Rosas
 Administrative Law Judge