OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

In the Matter of the Appeal of:	) OTA Case No. 18063339
BLAZO SREDANOVIC AND MARY SREDANOVIC	) Date Issued: August 16, 2019

OPINION

Representing the Parties:

For Appellants:	Blazo Sredanovic Mary Sredanovic
For Respondent:	Grace Power, Tax Counsel
For Office of Tax Appeals:	Sarah Fassett, Tax Counsel

R. TAY, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19324, Blazo Sredanovic and Mary Sredanovic ("appellants") appeal an action by the Franchise Tax Board ("FTB" or "respondent") denying appellants' claim for refund of $18,634.83 of interest paid for the 2015 tax year.

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

ISSUE

Whether appellants are entitled to interest abatement for the 2015 tax year.

FACTUAL FINDINGS

1. Appellants were residents of Menlo Park, California, until they moved to Hawaii on January 9, 2015. After they relocated to Hawaii, appellants sold their Menlo Park home on May 6, 2015.
2. Appellant-husband wrote a letter to respondent in June of 2015 requesting guidance as to how to report the gain from the sale of appellants' Menlo Park home. He asked:

> On May 6, 2015, I sold my house in California. Should I pay estimated capital gains taxes in Hawaii or in California?
>
> Considering that in 2015 we also purchased a property for the sole purpose to be our permanent residence, can I defer some of the taxes from the proceeds of sale of my house in California?

3. Respondent did not promptly respond to appellant-husband's letter, so he sent it a second time on July 10, 2015, this time by registered mail. In the cover letter accompanying his re-sent letter, appellant-husband noted that he had "tried to call a half a dozen times, but had no luck in speaking with a live person."

4. Respondent did not reply to appellant-husband's letters until October 26, 2015, when it sent him a letter advising him to call respondent at (800) 852-5711, its toll-free number for general assistance. Appellant-husband said he tried many times, without success, to speak with a live individual using that number and leaving messages.

5. Notwithstanding appellants' lack of success at obtaining timely tax advice from respondent, appellants timely filed a joint 2015 California Nonresident or Part-Year Resident Income Tax Return (FTB Form 540NR) and remitted full payment with their return. On that return, appellants reported the gain from the sale of their Menlo Park home as taxable, but they treated it as *non*-California source income. Appellants reported the gain to their state of residence, Hawaii, and paid taxes on the gain to that state.

6. In 2017, appellants finally obtained the tax advice they had sought from FTB two years earlier, when FTB sent appellants a letter dated September 18, 2017, notifying them that their 2015 California return was being audited. In its letter, FTB advised appellants, in pertinent part, that the gain from the sale of their Menlo Park home was subject to California income tax regardless of their out-of-state residence, and proposed increasing appellants' California tax liability by $288,941.

7. Appellants promptly responded to respondent's audit findings in a letter dated September 29, 2017, and agreed to the proposed additional tax liability of $288,941, but objected to the imposition of interest in light of FTB's failure to timely respond to appellants' repeated attempts to obtain guidance from FTB as to how to report the gain from the sale of their home. Respondent advised appellants that imposition of interest was mandatory, and concluded its audit.

8. Respondent issued a Notice of Proposed Assessment (NPA) on November 15, 2017, increasing appellants' income by the amount of gain on the sale of the Menlo Park home, and proposing additional tax of $288,941, plus applicable interest.
9. On December 5, 2017, respondent received appellants' Request for Abatement of Interest dated November 9, 2017, and a letter dated November 28, 2017, requesting interest abatement for the period from the date appellants sold their California residence (May 6, 2015) to the date of resolution of this matter. Respondent treated these letters as a protest of the NPA with respect to respondent's proposed interest assessment.
10. Appellants made a payment of $288,940 on January 2, 2018, which did not include payment of the applicable interest.
11. Respondent denied appellants' request for interest abatement in a letter dated March 15, 2018.
12. On May 11, 2018, respondent issued a Notice of Determination – Not to Abate Interest.
13. On May 29, 2018, respondent issued a 2015 Notice of State Income Tax Due reflecting a total amount remaining due of $18,634.83 of interest.
14. Appellants paid the interest amount due of $18,634.83 on May 29, 2018, and filed this timely appeal.

DISCUSSION

If any amount of tax is not paid by the due date, interest is required to be imposed from the due date until the date the taxes are paid. (R&TC, § 19101(a).) Imposition of interest is mandatory, and it can only be abated in certain limited situations when authorized by law.[1] (*Appeal of Amy M. Yamachi* (77-SBE-095) 1977 WL 3905.) Interest is not a penalty imposed on a taxpayer, it is merely compensation for the use of money, and there is no reasonable cause exception to imposition of interest. (*Appeal of Audrey C. Jaegle* (76-SBE-070) 1976 WL 4086; *Appeal of Yvonne M. Goodwin* (97-SBE-003) 1997 WL 258474.) The Office of Tax Appeals has jurisdiction to determine whether respondent's failure to abate interest under R&TC section 19104 was an abuse of discretion; if so, we may order an abatement of interest. (R&TC, § 19104(b)(2)(B); *Appeal of Ernest J. Teichert* (99-SBE-006) 1999 WL 1080256.)

[1] Other statutory interest abatement provisions are not applicable to the facts, and not discussed further.

Here, appellants' 2015 California tax was due in April 2016, but was not paid until January 2018. Consequently, respondent was required to impose interest on the balance due from the time the payment of tax was originally due until the time it was fully paid. Respondent's computation of the interest is not in dispute.

Appellants contend that they are entitled to interest abatement because of respondent's failure to timely answer their questions regarding whether the gain from their sale of the Menlo Park home should be included in their California or Hawaii taxable incomes.[2] Appellants sent letters in June and July 2015 to requesting advice on this subject. Respondent's response, dated October 26, 2015, did not provide the requested advice. It was not until September 18, 2017, when respondent notified appellants that their return was being audited, that respondent finally provided the advice they had requested two years earlier, informing them that the gain on the sale of the Menlo Park home was subject to California tax. Appellants contend that, if respondent had provided a timely answer to their inquiries, they would have reported the income to California on their timely filed return, and paid timely the appropriate California tax. They further contend that they are entitled to interest abatement because the late payment of tax was attributable to respondent's action or inaction, not theirs.

Courts have stated that abatement of interest is intended for circumstances where the failure to do so would be widely perceived as grossly unfair. (*Franklin v. Commissioner* (2008) T.C. Memo. 2008-13 [citing H. Rept. 99–426, at p. 844 (1985), 1986–3 C.B. (Vol. 2) 1, 844; S. Rept. 99–313, at p. 208 (1986), 1986–3 C.B. (Vol. 3) 1, 208].) Thus, the mere passage of time does not establish an unreasonable error or delay. (*Ibrahim v. Commissioner* (2011) T.C. Memo. 2011-215.) FTB may abate interest related to a deficiency or a proposed deficiency to the extent the interest is attributable in whole or in part to: (1) an unreasonable error or delay by an officer or employee of respondent in performing a ministerial or managerial act; (2) which occurred after respondent contacted the taxpayer in writing regarding the proposed assessment; and (3) provided no significant aspect of that error or delay is attributable to the taxpayer. (R&TC, § 19104(a)(1), (b)(1); *Appeal of Michael and Sonia Kishner* (99-SBE-007) 1999 WL 1080250.)

[2] Appellants note that they made a similar request to the Hawaii tax authorities and received a prompt response. That response, however, erroneously advised appellants to include the gain in their Hawaii income. It appears from the record that appellants either have obtained, or are in the process of obtaining, a refund of the Hawaii tax paid on the gain at issue.

A taxpayer must meet all three requirements before FTB is allowed to abate interest under R&TC section 19104.

Under R&TC section 19104, interest abatement is only potentially allowable for periods of time *after* FTB has contacted the taxpayer in writing with respect to that deficiency or payment. (R&TC, § 19104(b).) Here, respondent first contacted appellants in writing about the deficiency on September 18, 2017, when it informed appellants that it was opening an examination of appellants' 2015 tax return and referenced the proposed additional tax of $288,941. There is no statutory authority to abate the interest that accrued prior to this date (that is, for the period from April 15, 2016 to September 18, 2017). Appellants made full payment of their deficiency assessment on January 2, 2018, and thus, the only time period available for interest abatement is from September 18, 2017 to January 2, 2018. To obtain interest abatement for this period, appellants must show they meet the other requirements set forth in R&TC section 19104(a). Because appellants have not shown that they meet the requirements of R&TC section 19104(a)(1), they are not entitled to interest abatement.

Appellants do not meet the requirements of R&TC section 19104(a)(1) because respondent's failure to provide them with requested legal advice was not "an unreasonable error or delay . . . in performing a ministerial or managerial act." (R&TC, § 19104(a)(1); see also Int.Rev. Code, § 6404(e).) Although the R&TC does not define what is meant by an "unreasonable error or delay," or "a ministerial or managerial act," we look to the comparable federal statute, Internal Revenue Code section 6404 (e), and the regulations thereunder for guidance. (*Douglas v. State* (1948) 48 Cal.App.2d 835, 838; *Appeal of Michael and Sophia Kishner*, *supra*.)

Treasury Regulation section 301.6404-2(b) defines these terms as follows:

> (1) A ministerial act is 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.
>
> (2) Managerial act means an 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.

(Treas. Reg. § 301.6404-2(b)(1), (b)(2).)

Appellants contend that they are entitled to interest abatement because of respondent's failure to respond to their letters requesting tax advice. It is undisputed that appellants acted in good faith and took reasonable and prompt action to timely comply with their tax obligations. Respondent's responses to appellants' inquiries were neither timely nor helpful. However, respondent's failure to timely and substantively respond to appellants' tax questions does not constitute a failure to perform a ministerial or managerial act because preparing a proper response involved making a legal determination of the tax consequences of the sale of appellants' Menlo Park home. No matter how simple such a determination may be, it does not constitute a ministerial or managerial act. Thus, appellants are not entitled to interest abatement under R&TC section 19104.

This panel finds no other grounds to support appellants' request for interest abatement. R&TC section 21012 allows interest abatement in situations where a taxpayer relies on written advice from respondent. Here, however, no written advice was provided, so appellants cannot rely on R&TC section 21012 for interest abatement. Furthermore, there is no provision for interest abatement in R&TC section 21012 or FTB Notice 2009-08 based on respondent's failure to provide legal advice to a taxpayer.

Lastly, appellants contend that they are entitled to interest abatement because they did not have the use of the tax that was not paid to California, since the amount not paid to California (or a substantial portion thereof) was mistakenly paid as tax to Hawaii. However, appellants cite no authority for the proposition taxpayers do not owe interest on a tax deficiency if they did not earn interest on the amount not paid.[3] To qualify for interest abatement, appellants must show that they qualify under a statutory exception to the imposition of interest. This they have not done.

HOLDING

Appellants have not established that they are entitled to interest abatement.

[3] Furthermore, we presume that appellants will receive some interest on the refund of its Hawaii tax overpayment, although we do not base our denial of interest abatement on that fact.

DISPOSITION

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

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Richard I. Tay
Administrative Law Judge

We concur:

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Jeffrey I. Margolis
Administrative Law Judge

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Tommy Leung
Administrative Law Judge