

OFFICE OF TAX APPEALS
STATE OF CALIFORNIA

In the Matter of the Appeal of:) OTA Case No. 18042958
LCP VII HOLDINGS LP) Date Issued: November 20, 2019
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OPINION

Representing the Parties:

For Appellant: Thomas Giannetti, CFO

For Respondent: Gi Nam, Tax Counsel

For Office of Tax Appeals: Andrea Long, Tax Counsel

J. LAMBERT, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19324, LCP VII Holdings LP (appellant) appeals an action by the Franchise Tax Board (FTB) denying appellant’s claim for refund of \$1,264 for the 2011 tax year, \$1,064 for the 2012 tax year, \$1,080 for the 2013 tax year, and \$1,080 for the 2014 tax year.¹

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

ISSUE

Whether appellant has shown reasonable cause for failing to timely file its tax returns.

FACTUAL FINDINGS

1. Appellant is a foreign partnership with interests in entities both inside and outside of the United States.

¹ Appellant’s claim included a request for a refund of penalties and interest. However, appellant did not provide a specific contention alleging a basis for interest abatement and we find no apparent grounds for interest abatement under the facts. Appellant also provides no argument or evidence related to the imposition of the demand penalty, so it will not be discussed further.

2. Appellant did not file a 2011 return. FTB sent appellant a Demand for Tax Return (Demand) dated April 24, 2015, stating that it received information indicating that appellant may have a California filing requirement. The Demand required that by May 24, 2015, appellant file a 2011 return, explain why it was not required to file a return, or mail a copy of its return if it already filed a return.
3. After appellant did not timely respond to the Demand, FTB issued appellant a Notice of Proposed Assessment (NPA) for 2011 on August 14, 2015, which proposed an assessment of tax and penalties, plus interest.
4. On October 15, 2016, appellant filed partnership returns for the 2011 through 2014 tax years.
5. On its 2011 return, appellant reported California-source income of \$667,798 from pass-through entities and tax of \$800. FTB revised the amounts on the NPA and issued a notice imposing a late-filing penalty of \$200, a partnership late-filing penalty of \$864, and a demand penalty of \$200, plus interest, for the 2011 tax year.
6. On its 2012 return, appellant reported California-source income of \$5,894,139 from pass-through entities and tax of \$800. FTB issued a notice imposing a late-filing penalty of \$200 under R&TC section 19131 and a partnership late-filing penalty of \$864 under R&TC section 19172, plus interest, for the 2012 tax year.
7. On its 2013 return, appellant reported California-source income of \$7,996,152 from pass-through entities and tax of \$800. FTB issued a notice imposing a partnership late-filing penalty of \$1,080 under R&TC section 19172, plus interest, for the 2013 tax year.
8. On its 2014 return, appellant reported California-source income of \$6,134,247 from pass-through entities and tax of \$800. FTB issued a notice imposing a partnership late-filing penalty of \$1,080 under R&TC section 19172, plus interest, for the 2014 tax year.
9. Appellant paid the balance due and filed a claim for refund for penalties and interest, but not for any tax. FTB denied the claim and this timely appeal followed.

DISCUSSION

R&TC section 17935(a) generally provides that every limited partnership “doing business” in California within the meaning of R&TC section 23101 shall pay an annual tax. And R&TC section 18633(a)(1) provides that that every partnership doing business in California has

to file its tax return on or before the 15th day of the fourth month following the close of its tax year.

Appellant filed returns for all of the years at issue, but they were filed late. Hence late-filing penalties were imposed by FTB pursuant to R&TC sections 19131 and 19172. Although appellant does not seek a refund of the annual minimum tax amounts it paid with its returns for the years at issue, it contends that the late-filing penalties should be abated. A late-filing penalty imposed under R&TC section 19131 will be abated if the taxpayer shows that the failure to timely file was due to reasonable cause and not due to willful neglect.² A late-filing penalty imposed under R&TC section 19172 will be abated if the taxpayer shows that the failure to timely file was due to reasonable cause. To establish reasonable cause, the taxpayer must show that the failure to timely file occurred despite the exercise of ordinary business care and prudence, or that such cause existed as would prompt an ordinary intelligent and prudent businessperson to have so acted under similar circumstances. (*Appeal of Tons* (79-SBE-027) 1979 WL 4068.)

Appellant contends that it had reasonable cause for its failure to timely file returns because it believed that it was not “doing business” in California within the meaning of R&TC section 23101 and under the California Court of Appeals decision in *Swart Enterprises, Inc. v. Franchise Tax Bd.* (2017) 7 Cal.App.5th 497 (*Swart*). Appellant notes that it was only a limited partner in pass-through entities, it was not registered to do business here, it did not operate any California trade or business, and claims that the statutes defining the term “doing business” are unclear.

We disagree. “Doing business” is defined in R&TC section 23101. It contains alternative tests for determining whether a taxpayer is doing business in this state. If any of the alternative tests are met, the taxpayer is doing business in this state and must file a California return.

² There is no allegation that appellant’s failure to timely file was due to willful neglect; hence, we do not address that aspect of the standard.

Under the factor threshold tests set forth in R&TC section 23101(b)(2), if a taxpayer has sales in this state for the applicable tax year that exceed the lesser of \$500,000 or 25 percent of the taxpayer's total sales, the taxpayer is found to be "doing business" in California.³ (R&TC, § 23101(b)(2).) Appellant reported California-source income from pass-through entities exceeding the required threshold for the years at issue.⁴ It is reasonable for us to assume that appellant's California gross receipts would have been equal to or would exceed its California-source income, given that appellant's California-source income, unlike gross receipts, would have been reduced by any losses incurred in California. Furthermore, appellant does not dispute that it meets the gross receipts threshold, and was provided the opportunity to submit evidence to show its actual gross receipt amounts in California, but failed to do so. Because appellant was doing business in California within the meaning of R&TC section 23101(b)(2), appellant had a California filing requirement for the years at issue.

Appellant argues that the decision in *Swart, supra*, supports a conclusion that it was not "doing business" in California. However, the decision in *Swart* was based upon the test for "doing business" under R&TC section 23101(a), and not R&TC section 23101(b)(2), as is applicable to this appeal. Therefore, *Swart* does not apply here.

Although appellant argues that it was unaware of its filing requirement due to its interpretation of the requirements for "doing business" in California, ignorance of the law does not excuse compliance with statutory requirements. (*Appeal of Diebold, Inc.* (83-SBE-002) 1983 WL 15389.) Appellant did not exercise ordinary business care and prudence when it failed to acquaint itself with the California tax law requirements. (*Id.*) Therefore, appellant has not shown reasonable cause for the late filing of the returns.

³ For taxable years beginning on or after January 1, 2011, "sales" means all gross receipts of the taxpayer not allocated under R&TC sections 25123 to 25127, inclusive. "Gross receipts" means the gross amounts realized on the sale or exchange of property, the performance of services, or the use of property or capital in a transaction that produces business income, in which the income, gain, or loss is recognized under the Internal Revenue Code. (R&TC, § 25120(f).)

⁴ The sales threshold is required to be adjusted annually based on an inflation adjustment factor. Therefore, the sales threshold amounts for the appeal years are the lesser of 25 percent of sales or: (1) \$500,000 for 2011; (2) \$509,500 for 2012; (3) \$518,162 for 2013; and (4) \$529,562 for 2014. (R&TC, § 23101(b)(2) & (c)(1).) Appellant's California-source income for the years at issue was: (1) \$667,798 for 2011; (2) \$5,894,139 for 2012; (3) \$7,996,152 for 2013; and (4) \$6,134,247 for 2014.

HOLDING

Appellant has not shown reasonable cause for failing to timely file its tax returns.

DISPOSITION

FTB’s action is sustained.

DocuSigned by:
Josh Lambert
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Josh Lambert
Administrative Law Judge

We concur:

DocuSigned by:
Jeffrey I. Margolis
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Jeffrey I. Margolis
Administrative Law Judge

DocuSigned by:
Suzanne B. Brown
47F45ABE89E34D0...
Suzanne B. Brown
Administrative Law Judge