

OFFICE OF TAX APPEALS
STATE OF CALIFORNIA

In the Matter of the Appeal of:)
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BRAYTON KIKUMOTO PROPERTIES, LLC)
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) OTA Case No. 18011187
)
) Date Issued: July 26, 2019

OPINION

Representing the Parties:

For Appellant: John Brayton, Principal
For Respondent: Joel Smith, Tax Counsel
Marguerite Mosnier, Tax Counsel IV

For Office of Tax Appeals: Neha Garner, Tax Counsel III

K. GAST, Administrative Law Judge: Pursuant to California Revenue and Taxation Code (R&TC) section 19324(a), Brayton Kikumoto Properties, LLC (appellant) appeals actions by respondent Franchise Tax Board (FTB) in denying appellant’s claims for refund for tax years 2012 and 2013.

Office of Tax Appeals (OTA) Administrative Law Judges Kenneth Gast, Alberto T. Rosas, and Linda C. Cheng held an oral hearing for this matter in Los Angeles, California, on May 21, 2019. At the conclusion of the hearing, the record was closed and this matter was submitted for decision.

ISSUES¹

1. For the 2012 and 2013 tax years, has appellant established reasonable cause to abate the late-filing penalty imposed under R&TC section 19172?
2. For the 2012 and 2013 tax years, was the late payment penalty properly imposed under R&TC section 19132, and if so, has appellant established reasonable cause to abate it?

FACTUAL FINDINGS

1. During the tax years at issue, appellant was a two-member, member-managed, limited liability company (LLC) that was formed in California. Mr. John Brayton, appellant's representative in this matter, was one of its two members. He was responsible for ensuring the timely filing and payment of its taxes.
2. Appellant untimely filed its 2012 Form 568 on June 29, 2015, which was over two years past the filing due date of April 15, 2013. FTB imposed a late-filing penalty of \$432 under R&TC section 19172.
3. Appellant also did not pay its 2012 annual \$800 minimum LLC tax by the payment due date of April 15, 2012. FTB applied appellant's \$600 overpayment credit from the previous tax year to the 2012 tax year. This left a \$200 balance due that appellant untimely paid effective April 15, 2013, the filing due date of its 2012 tax return. FTB imposed a late payment penalty of \$22 under R&TC section 19132.
4. Appellant untimely filed its 2013 Form 568 on October 7, 2015, which was about a year and a half past the filing due date of April 15, 2014. FTB imposed a late-filing penalty of \$432 under R&TC section 19172.

¹ In its appeal letter dated July 7, 2017, appellant also appealed the denial of its refund claims for the 2010 and 2011 tax years related to late-filing and/or late payment penalties. FTB denied appellant's refund claim for these years in a Notice of Action dated March 17, 2017. Appellant had 90 days from March 17, 2017, or until June 15, 2017, to appeal the denial to the Board of Equalization (BOE), our predecessor agency. However, appellant did not file an appeal until July 7, 2017. Therefore, we do not have jurisdiction over those years. We note the BOE previously communicated this conclusion to appellant in a letter dated September 11, 2017, a copy of which was provided to appellant at the oral hearing.

Also, in its appeal letter, appellant requested a refund of late payment penalties it believed were paid for the 2014 tax year. However, we do not need to address whether this refund request was timely filed or appealed, because at the oral hearing appellant conceded the 2014 tax year is no longer in dispute. Accordingly, the tax years on appeal to OTA are properly limited to the 2012 and 2013 tax years.

5. Appellant also did not pay its 2013 annual \$800 minimum LLC tax by the payment due date of April 15, 2013. Rather, appellant untimely paid it effective April 15, 2014, the filing due date of its 2013 tax return. FTB imposed a late payment penalty of \$88 under R&TC section 19132.
6. After paying the penalties, appellant filed two separate refund claims for the 2012 and 2013 tax years. Appellant requested abatement of both the late-filing and late payment penalties due to Mr. Brayton's illness.
7. FTB denied the claims. This timely appeal followed.

DISCUSSION

Issue 1 – For the 2012 and 2013 tax years, has appellant established reasonable cause to abate the late-filing penalty imposed under R&TC section 19172?

R&TC section 19172 imposes a late-filing penalty when a partnership (or an LLC classified as a partnership) fails to file a return at the time prescribed (determined with regard to any extension of time for filing), unless it is shown that the failure was due to reasonable cause. Here, for the 2012 and 2013 tax years, appellant does not dispute whether this penalty was properly imposed or computed. Rather, appellant asserts reasonable cause exists to abate the penalty.

To establish reasonable cause, “the taxpayer must show that the failure to file timely returns occurred despite the exercise of ordinary business care and prudence, or that such cause existed as would prompt an [ordinarily] intelligent and prudent businessman to have so acted under similar circumstances.” (*Appeal of Tons* (79-SBE-027) 1979 WL 4068.) A late-filing penalty imposed by FTB is presumed to be correct, and the burden of proof is on the taxpayer to establish that reasonable cause exists to support an abatement of the penalty. (*Ibid.*) Unsupported assertions are insufficient to satisfy a taxpayer's burden of proof. (*Appeal of Magidow* (82-SBE-274) 1982 WL 11930.)

The standard for reasonable cause based on illness is a high one. While significant illness or other personal difficulties may constitute reasonable cause, taxpayers must present credible and competent proof that despite the exercise of ordinary business care and prudence, they were continuously prevented from timely filing a return. (*Appeal of Halaburka* (85-SBE-025) 1985 WL 15809; *Appeal of Seaman* (75-SBE-080) 1975 WL 3564.) “Reasonable cause requires a

showing of incapacity; ‘selective inability’ to file tax returns while attending to other responsibilities does not demonstrate reasonable cause.” (*Wright v. Commissioner*, T.C. Memo. 1998-224, 1998 WL 331470 at *5, citations omitted.) In addition, “the duration of the incapacity must approximate that of the failure to file.” (*Ibid.*) However, where personal difficulties simply caused taxpayers to sacrifice the timeliness of one aspect of their affairs to pursue other aspects, taxpayers must bear the consequences of that choice. (*Appeal of Halaburka, supra; Appeal of Orr* (68-SBE-010) 1968 WL 1640.)

On appeal, appellant contends that Mr. Brayton, who was the member responsible for its tax matters, was mentally and physically incapacitated during the time period its returns became due. This caused Mr. Brayton to untimely file appellant’s 2012 and 2013 tax returns. Arguing on behalf of appellant, Mr. Brayton claims his illness, which severely affected him both physically and mentally, started in 2010 or 2011, but was not treated until its diagnosis in 2014 or later. As his illness progressed, his ability to track details became difficult, if not impossible. He acknowledges that, during his illness, he was able to pay appellant’s 2012 and 2013 annual \$800 minimum taxes by the original due date of those returns. However, he asserts he could not do more complex tasks, such as file the returns on time. He maintains he could not delegate the filing responsibility to appellant’s only other member, his business partner, who was usually out of the country, unaware of, and ultimately not responsible for appellant’s tax obligations. He claims that, in hindsight, he may have been able to delegate the responsibility to a tax professional, but this was not apparent to him when he was sick. Finally, he asserts this same illness, among other things, caused him to untimely file his own personal income taxes.

However, the evidentiary record does not show reasonable cause has been established for three main reasons. First, and most importantly, Mr. Brayton was gainfully employed during 2013 and 2014, earning employee wages of \$61,377 and \$59,613, respectively. Mr. Brayton testified that he was working as a full-time employee from October 2012 through February 2015. Therefore, we find Mr. Brayton’s illness did not incapacitate him to such an extent that he was unable to file appellant’s 2012 and 2013 returns during 2013 and 2014, respectively. (See, e.g., *Marrin v. Commissioner*, T.C. Memo. 1997-24, *affd.* (2d Cir. 1998) 147 F.3d 147 [reasonable cause for late-filing not found where taxpayer was a full-time employee and was also actively transacting business in the securities market despite claimed depression].)

Second, while the hospital appointment records and doctor's notes submitted during this appeal undisputedly show Mr. Brayton was sick over the course of many years, they do not show he was continuously prevented from timely filing appellant's returns. For example, appellant submitted a note from one of his doctors, dated July 24, 2014, in which his doctor "advised" him to decrease his work hours to roughly 40 hours a week. This indicates that even though Mr. Brayton may have been experiencing stress-related health issues, they were not impeding his ability to work, and therefore did not, in our view, hinder his ability to timely complete and file tax returns.

Third, we believe a reasonably prudent businessperson, who was unable to fulfill his tax duties due to health issues, would have promptly communicated this to his partner or, at the very least, delegated the work to a tax professional. Mr. Brayton testified that the intent of the business arrangement was to have one member responsible for meeting the tax obligations of appellant, which was essentially a defunct entity that never conducted business. He further testified that he told the other member that appellant's taxes were being filed and paid—and, at the time, he thought they were—but the other member was unaware of the extent of his health issues.

However, Mr. Brayton was aware of appellant's tax obligations during the appeal years. This is evidenced by two checks he wrote on behalf of appellant: (1) one for \$800 effective April 15, 2013, the day the 2012 return was due; and (2) the other for \$1,300 effective April 15, 2014, the day the 2013 return was due. Therefore, we believe Mr. Brayton, despite his sickness, still had the mental faculty to seek assistance from the other member or a third-party tax professional to help him timely file appellant's returns.

In sum, as he testified at the hearing, Mr. Brayton "prioritized" certain aspects of his personal life over appellant's tax obligations. Appellant must bear the consequences of his choices. Accordingly, appellant has not established reasonable cause to abate the late-filing penalty for the 2012 and 2013 tax years.

Issue 2 – For the 2012 and 2013 tax years, was the late payment penalty properly imposed under R&TC section 19132, and if so, has appellant established reasonable cause to abate it?

R&TC section 17941(c) provides that the annual \$800 minimum tax imposed on LLCs is due "on or before the 15th day of the *fourth month of the taxable year.*" (Emphasis added.) The \$800 tax, therefore, is due in the actual tax year, and not by the due date of the return, which is

generally the following year. On appeal, Mr. Brayton argues that he timely paid the annual minimum taxes on behalf of appellant for both the 2012 and 2013 tax years. To be considered timely, appellant's \$800 taxes for the 2012 and 2013 tax years must have been paid by April 15, 2012 and April 15, 2013, respectively. However, appellant undisputedly did not pay the taxes until the following years, on April 15, 2013 and April 15, 2014, which are the filing—*not payment*—due dates for 2012 and 2013 tax years, respectively. Accordingly, appellant untimely paid the \$800 taxes for these years.

R&TC 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. Here, because the annual \$800 minimum tax was untimely paid, we find the late payment penalty was properly imposed and computed for both the 2012 and 2013 tax years. Because FTB does not assert willful neglect is present in this case, the only remaining issue is whether appellant has demonstrated reasonable cause for the late payments.

The late payment penalty may be abated if the taxpayer can show that the failure to make a timely payment of tax was due to reasonable cause. (R&TC, § 19132(a).) To establish reasonable cause for the late payment of tax, the taxpayer must show that the failure to make a timely payment of the proper amount of tax occurred despite the exercise of ordinary business care and prudence. (*Appeal of Sleight* (83-SBE-244) 1983 WL 15615.) The taxpayer bears the burden of proving reasonable cause exists. (*Ibid.*) The late-filing and the late payment penalties generally deal with the same questions and weigh the same evidence for purposes of making reasonable cause determinations. (*Appeal of Berolzheimer* (86-SBE-172) 1986 WL 22860.)

Here, appellant presents the same arguments to contend reasonable cause exists to abate the late payment penalties as it does for the late-filing penalties. However, for the reasons expressed above, the evidence does not demonstrate appellant's failure to timely pay its taxes was due to reasonable cause. (See, e.g., *Appeal of Triple Crown Baseball LLC*, 2019-OTA-025P, Feb. 12, 2019 [reasonable cause for limited liability company's late payment not found where its sole member, who suffered an accident, was still able to earn income].)


HOLDINGS

1. For the 2012 and 2013 tax years, appellant has not established reasonable cause to abate the late-filing penalty.

- 2. For the 2012 and 2013 tax years, the late payment penalty was properly imposed, and appellant has not established reasonable cause to abate it.

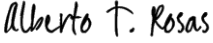
DISPOSITION

FTB’s actions denying appellant’s refund claims are sustained.


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 Kenneth Gast
 Administrative Law Judge

We concur:

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 Alberto T. Rosas
 Administrative Law Judge

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 Linda C. Cheng
 Administrative Law Judge