

OFFICE OF TAX APPEALS
STATE OF CALIFORNIA

In the Matter of the Appeal of:) OTA Case No. 20066249
D. WALLINGA AND)
M. WALLINGA)
_____)

OPINION

Representing the Parties:

For Appellants: Vic Abajian, Abajian Law
Aksel Bagheri, Abajian Law

For Respondent: Eric A. Yadao, Tax Counsel III

H. LE, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19324, D. Wallinga and M. Wallinga (appellants) appeal an action by Franchise Tax Board (respondent) denying appellants’ claim for refund of \$5,795.50 for the 2016 tax year.

Appellants waived their right to an oral hearing; therefore, we decide this matter based on the written record.

ISSUES

1. Whether respondent properly imposed the notice and demand penalty (demand penalty).
2. Whether appellants have established reasonable cause to abate the demand penalty.

FACTUAL FINDINGS

1. On May 8, 2018, respondent issued to appellants¹ a Demand for Tax Return (2016 Demand) because its records indicated that appellants’ 2016 California resident income tax return had not been filed and appellants had received sufficient income to trigger a filing obligation. The 2016 Demand required appellants to respond by a specific date, by either filing a 2016 tax return, providing evidence that a return had already been filed, or

¹ For convenience, we are referring to appellants even though respondent’s notices only listed appellant-husband.

- providing information on why they were not required to file a return. Appellants did not respond.
2. Subsequently, on July 9, 2018, respondent issued a Notice of Proposed Assessment (2016 NPA), which proposed to assess tax (based on income reported by an employer), and, among other things, the demand penalty of \$6,792. Appellants did not protest the 2016 NPA, and the assessment became due and payable.
 3. Respondent then issued a Notice of State Income Tax Due, which appellants paid.
 4. Appellants subsequently filed a late joint 2016 tax year return, which respondent accepted and processed. Based on the reduced tax reported by appellants, respondent reduced the demand penalty from \$6,792 to \$5,795.50.
 5. Appellants filed a claim for refund, requesting abatement of the demand penalty.
 6. Respondent denied the claim for refund, and this timely appeal followed.
 7. As relevant to the demand penalty issue here, respondent previously issued a Request for Tax Return (Request) dated July 18, 2017, for appellants' 2014 tax return (2014 Request). After appellants failed to respond, respondent issued an NPA (2014 NPA) dated September 18, 2017. Respondent also previously issued a Request dated June 15, 2017, for appellants' 2015 tax return (2015 Request), which appellants also failed to respond to, resulting in an NPA (2015 NPA) dated August 14, 2017.

DISCUSSION

Issue 1: Whether respondent properly imposed the demand penalty.

R&TC section 19133 imposes a penalty when a taxpayer fails to file a return or provide information upon respondent's notice and demand to do so, unless the failure is due to reasonable cause and not willful neglect. For individuals, respondent will only impose a demand penalty if two conditions are satisfied: (1) the taxpayer fails to respond to a current Demand; and (2) at any time during the preceding four tax years, respondent issued an NPA following the taxpayer's failure to timely respond to a Request or a Demand. (Cal. Code Regs., tit. 18, § 19133(b)(1)-(2).)

Illustrating this rule are two examples in California Code of Regulations, title 18, (Regulation) section 19133(d). Example 1 assumes that a taxpayer has failed to file a California income tax return for the 1999 tax year and that respondent mailed to the taxpayer a Request for

the 1999 tax year on January 15, 2001. The taxpayer failed to respond to this Request, and respondent issued an NPA on March 20, 2001, assessing tax, a late-filing penalty, and interest, but no demand penalty. Example 2 continues under the same facts as Example 1, except that the taxpayer has also failed to file a return for the 2001 tax year. Respondent issued a Demand for the 2001 tax year and the example concludes that respondent will impose the demand penalty if the taxpayer fails to respond because the taxpayer received an NPA for not filing a return within the previous four years.

However, an inconsistency develops in concurrently applying the second condition above and Example 2 to this appeal's facts. Here, respondent issued both the 2014 and 2015 Requests and NPAs in 2017, after the 2016 tax year. Therefore, respondent did not propose an assessment, after appellants failed to timely respond to the 2014 and 2015 Requests, *during* one of the four tax years preceding the 2016 tax year at issue (i.e., 2012 through 2015). Thus, it would appear the second condition under Regulation section 19133(b)(2) has not been met. Nevertheless, according to Example 2 and consistent with the regulation's intent, as discussed below, the demand penalty's imposition is warranted because appellants received an NPA for previously failing to timely file their 2014 and 2015 tax returns, which are both tax years that fall within the four tax years preceding 2016.

This interpretation is supported by the intent of Regulation section 19133, which is to impose the demand penalty only upon individual taxpayers who are repeat nonfilers; that is, those taxpayers who received an NPA for previously failing to timely file for any one of the preceding four taxable years.² In keeping with the drafters' intent, the language in Example 2 should control.

Here, both conditions under Regulation section 19133(b) are satisfied. As to the first condition, appellants failed to timely respond to the 2016 Demand.³ As to the second condition,

²“Under this proposed regulation, the Franchise Tax Board defines a repeat nonfiler as an individual who has received a proposed assessment of tax after receiving and failing to respond to either a request for tax return or a demand for tax return within the previous four years. The Franchise Tax Board has also determined that four years is a reasonable period of time to look back in making a determination as to whether a taxpayer is a repeat nonfiler.” (Cal. Reg. Notice Register 2004, No. 17-Z, p. 504.)

³ Appellants also argue that respondent did not properly send the 2016 Demand to appellants. However, respondent addressed the 2016 Demand to the same address as listed on appellants' late-filed 2016 return. Appellants have not demonstrated that respondent failed to send the 2016 Demand to appellants' last known address. (See *Appeal of Floria* (83-SBE-003) 1983 WL 15390.)

appellants failed to timely respond to the 2014 and 2015 Requests, and as a result, respondent issued NPAs for both the 2014 and 2015 tax years, either tax year of which falls within the four tax years preceding the 2016 tax year at issue. Thus, respondent properly imposed the demand penalty for the 2016 tax year.

Issue 2: Whether appellants have established reasonable cause to abate the demand penalty.

When respondent imposes a demand penalty, the law presumes that respondent's action was correct. (*Appeal of Wright Capital Holdings LLC*, 2019-OTA-219P.) The burden of proof is on the taxpayer to show that reasonable cause exists to support the penalty's abatement. (*Ibid.*) To establish reasonable cause, a taxpayer must show that the failure to reply to the notice and demand or to the request for information occurred despite the exercise of ordinary business care and prudence. (*Ibid.*)

Here, appellants provided no arguments and evidence to support reasonable cause for failure to respond to the 2016 Demand.

HOLDINGS

1. Respondent properly imposed the demand penalty.
2. Appellants have not established reasonable cause to abate the demand penalty.

DISPOSITION

We sustain respondent’s denial of appellants’ refund claim in full.

DocuSigned by:

Huy "Mike" Le

Huy "Mike" Le
Administrative Law Judge

I concur:

DocuSigned by:

Natasha Ralston

Natasha Ralston
Administrative Law Judge

C. AKIN, dissenting:

I respectfully dissent with respect to Issue 1 and, for that reason, would not have reached Issue 2. As explained below, I would have found Franchise Tax Board (respondent) improperly imposed the notice and demand penalty (demand penalty) under Revenue and Taxation (R&TC) section 19133 for the 2016 tax year.

R&TC section 19133 provides that if a taxpayer fails to file a return upon notice and demand by respondent, then respondent may impose a penalty of 25 percent of the amount of tax assessed pursuant to R&TC section 19087, unless the failure is due to reasonable cause and not willful neglect. California Code of Regulations, title 18, (Regulation) section 19133 further provides that for individuals, the demand penalty will only be imposed if the following two conditions are satisfied:

- (1) the taxpayer fails to timely respond to a current Demand for Tax Return in the manner prescribed, and
- (2) the FTB has proposed an assessment of tax under the authority of Revenue and Taxation Code section 19087, subdivision (a), after the taxpayer failed to timely respond to a Request for Tax Return or a Demand for Tax Return in the manner prescribed, *at any time during the four-taxable-year period preceding the taxable year for which the current Demand for Tax Return is issued.*

(Cal. Code Regs., tit. 18, § 19133(b)(1)-(2), emphasis added.)

Under the plain and unambiguous language of subsection (b)(2) above, I find, contrary to the majority’s conclusion, that this subsection requires the Notice of Proposed Assessment (NPA) for a prior tax year to have been issued “*at any time during the four-taxable-year period preceding*” the current tax year for which respondent seeks to impose the demand penalty. Here, to properly impose the demand penalty for the 2016 tax year, respondent’s regulation requires that respondent have issued an NPA for a prior tax year on a date anytime between January 1, 2012, through December 31, 2015. This threshold requirement has not been met in this case.

Specifically, rather than being issued “*at any time during the four-taxable-year period preceding the taxable year for which the current Demand for Tax Return is issued,*” the NPAs for the 2014 and 2015 tax year were not issued until September 18, 2017, and August 14, 2017,

respectively, which is *after* the 2016 tax year “for which the current Demand for Tax Return is issued.” Therefore, respondent improperly imposed the demand penalty.

I note that Example 2 of the regulation appears to interpret subsection (b)(2) as being met if the prior NPA were issued for a tax year “within the previous four years.” On this ground, the example contemplates the imposition of the demand penalty for the 2001 tax year where the prior NPA for the 1999 tax year was issued on a date during the 2001 tax year. Thus, the example imposes the demand penalty when the prior NPA was issued during the *same* tax year for which the current demand is issued. However, this example would not apply to the facts of this appeal as the prior NPAs were not issued during the same tax year for which the current demand is issued and were instead issued in 2017 *after* the 2016 tax year “for which the current Demand for Tax Return is issued.”

While respondent’s regulation is internally inconsistent in that the example is contrary to the operative language of the regulation,⁴ the operative language of the regulation is unambiguous. It carefully and precisely references “the four-taxable-year period preceding” the tax year for which the current Demand for Tax Return is issued. Rather than interpreting the operative language of the regulation, the example appears to overlook or disregard that language. As such, I would not place greater weight on the implication of the example than on the clear and precise operative language. Indeed, Regulation section 19133(d), where Example 2 is found, clearly indicates that the “examples are intended to *illustrate* the provisions of this regulation,” and thus, in my view, are not intended to be given greater weight than the rules themselves. (Emphasis added.) Therefore, I would resolve the internal conflict in respondent’s regulation by finding that respondent is bound by the ordinary and unambiguous meaning of the words used in the governing language of its regulation.


Finally, while “examples set forth in regulations remain persuasive authority *so long as they do not conflict with the regulations themselves*” (*Cook v. Commissioner* (7th Cir. 2001) 269 F.3d 854, 858, emphasis added), here, Example 2 does create such a conflict and I would not give it persuasive authority. Accordingly, because the words “at any time during” are

⁴ The example is contrary to the operative language because it would impose a demand penalty where the prior NPA was issued during the *same* tax year, while the operative language requires the NPA to have been issued “at any time during the four-taxable-year period *preceding* the taxable year for which the current Demand for Tax Return is issued.” (Emphasis added.)

unambiguous, respondent's interpretation ignoring this plain language should not be entitled to deference. (See *Kisor v. Wilkie* (June 26, 2019, No. 18-15) ___U.S.___[139 S.Ct. 2400, 2415].)

For the foregoing reasons, I respectfully dissent with respect to Issue 1 and, for that reason, would not have reached Issue 2.

DocuSigned by:


Cheryl E. Akin
Administrative Law Judge

Date Issued: 3/29/2021