**OFFICE OF TAX APPEALS**

**STATE OF CALIFORNIA**

| | |
|---|---|
| In the Matter of the Appeal of:<br>**B. BUTLER AND**<br>**V. BUTLER** | ) OTA Case No. 19075000<br>)<br>)<br>)<br>)<br>) |

# OPINION

Representing the Parties:

For Appellants: Yuki Hirai, Tax Appeals Assistance Program (TAAP)[1]

For Respondent: Anne Mazur, Specialist

N. RALSTON, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19324, B. Butler and V. Butler (appellants) appeal an action by the respondent Franchise Tax Board denying appellants' claim for refund of $1,311.50 for the 2016 tax year.

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

## ISSUE

Whether appellants have shown that the late filing of their 2016 return was due to reasonable cause and not willful neglect.

## FACTUAL FINDINGS

1. Appellants were nonresidents of California in 2016 but received California-sourced, pass-through income from a limited liability company (LLC).
2. The LLC timely filed an original tax return in California (Form 568) on February 27, 2017. While the LLC reported an address in Connecticut, it reported all of its income as California-sourced income. The California Schedule K-1 attached to the

[1] Appellant, B. Butler filed his opening brief. Mounia Boukhalfa of TAAP filed appellants' reply brief and Jonathan Dean of TAAP filed appellants' supplemental brief.

return similarly reported appellant-husband's share of the LLC income as being California-sourced income.

3. In 2016, appellant-husband sold his interest in the LLC to his partner. After the sale, the LLC's new accountant amended the LLC's 2016 California return, revising the California-sourced income reported on the LLC's original return.
4. In August of 2018, appellants received an amended Schedule K-1 revising appellant-husband's California-sourced-income from the LLC.
5. Appellants filed a joint California nonresident tax return for 2016 on September 7, 2018.
6. Respondent subsequently reviewed appellants' return and imposed a late-filing penalty of $3,210.50.
7. Appellants requested waiver of the penalty asserting that they had reasonable cause for filing late, which respondent denied.
8. On March 1, 2019, appellants filed an amended California return for 2016, which requested a refund of $7,596.
9. Respondent granted a portion of appellants' refund in the amount of $6,043.[2]
10. On April 15, 2019, respondent received appellants' claim for refund of the late-filing penalty based on reasonable cause.
11. Respondent denied appellants' claim for refund and this timely appeal followed.

## DISCUSSION

When respondent imposes a penalty, the law presumes that the penalty was imposed correctly. (*Appeal of Xie*, 2018-OTA-076P.) The burden of proof is on the taxpayer to show that reasonable cause exists to support an abatement of the penalty. (*Ibid*.) To overcome the presumption of correctness attached to the penalty, the taxpayer must provide credible and competent evidence supporting a claim of reasonable cause; otherwise, the penalty cannot be abated. (*Ibid*.) Section 19131 imposes a late-filing penalty on a taxpayer who fails to file a return by either the due date or the extended due date unless it is shown that the failure was due to reasonable cause and not willful neglect. The late-filing penalty is calculated at 5 percent of the tax for each month or fraction thereof that the return is late, with a maximum penalty of 25 percent of the tax.

[2] The refund amount reflects the revised tax liability of $5,246 as shown on appellants' amended return, a reduction to the late-filing penalty, and adjustments for interest.

The penalty may be abated if the taxpayer shows that the failure to timely file the return was due to reasonable cause and not due to willful neglect. (R&TC, § 19131(a).) The taxpayer bears the burden of proving that an ordinarily intelligent and prudent businessperson would have acted similarly under the circumstances. (*Appeal of Moren*, 2019-OTA-176P).[3] Willful neglect is defined as a conscious, intentional failure or reckless indifference. (*United States v. Boyle* (1985) 469 U.S. 241, 245). Reliance on a tax professional's advice for questions of substantive tax law, such as whether a liability exists, may constitute reasonable cause, where certain conditions are met, including where the tax professional has competency in the subject tax law and the tax professional's advice is based on the taxpayer's full disclosure of the relevant facts and documents. (*Ibid.*) By contrast, reliance on an expert cannot function as a substitute for compliance with an unambiguous statute. (*Ibid.*) Further, in *Appeal of Berolzheimer* (86-SBE-172) 1986 WL 22860, the Board of Equalization found that there was no basis in the record for concluding that the New York law firm retained by the appellants in that case had expertise in California tax law and therefore declined to hold, as a matter of law, that relying on an out-of-state law firm constituted reasonable cause for failing to comply with California's tax laws.

Appellants filed their 2016 return on September 7, 2018, more than a year after the due date for the return. Thus, the only question before us is whether appellants had reasonable cause for the late filing of their return so that the penalty may be abated. Appellants contend that they have established reasonable cause because they relied on their tax preparer who provided them with the erroneous advice that they did not have a California filing requirement. Appellants assert that their tax preparer was an Enrolled Agent who had expertise in the field of taxation and was "empowered by the U.S. Department of the Treasury." Appellants further assert that they fully disclosed the relevant documents and facts to their preparer. In support, appellants provide two letters from their tax preparer. In the first letter dated November 29, 2018, the tax preparer explains that the liability arose from an amended Schedule K-1 and that the 2016 California tax return was filed and paid as soon as the taxpayer received the amended K-1 form. In the letter dated November 13, 2019, the tax preparer notes that appellants' California return was filed after the original due date because, "prior to the amended K-1 in my opinion there was no tax due."

[3] For purposes of the facts and issue in this appeal, an analysis of whether there is reasonable cause for a failure to timely file a tax return is substantially the same as an analysis of whether there is reasonable cause for a failure to timely pay tax. Thus, authorities, persuasive or controlling, in one analysis may be equally persuasive or controlling in the other. (See *Appeal of Moren*, *supra*; *Appeal of Triple Crown Baseball*, *LLC*, 2019-OTA-025P.)

As noted above, in order to show that they had reasonable cause for their late filing, appellants must establish that their reliance on their tax professional's advice for questions of substantive tax law was reasonable. Here, appellants have failed to do so. Namely, appellants have failed to show that their tax preparer had competency in California tax law. Appellants' tax preparer, who was based in Connecticut during the period at issue, filed a timely return for the LLC for the 2016 tax year, including a Schedule K-1 for appellant-husband reporting California source income. Although the LLC return contained errors that were subsequently amended by another tax preparer, both the original and amended returns clearly indicated a California tax obligation for appellants.[4] Despite the fact that he prepared an LLC return and Schedule K-1 indicating that appellant-husband had California-sourced pass-through income from the LLC, appellants' tax preparer advised appellants that they did not have a California filing requirement. We would expect a tax preparer with competency in California tax law to advise appellants to file a California return where the available information so clearly indicated a California filing requirement. Therefore, we find that appellants have not established that they had reasonable cause for their late filing based on advice given by their tax professional.

Although the foregoing is dispositive, we note that appellants also provided a copy of a recent nonprecedential OTA decision, *Appeal of Thiede*, 2020-OTA-092, arguing that the present matter is analogous to the factors presented in that case. While *Thiede* has not been deemed precedential and therefore, is not binding on this panel, we note that the facts in *Thiede* are distinguishable from the present matter. In *Thiede* it is not clear whether the CPA firm that the appellant relied upon was based in California but neither the parties nor the panel raised any concerns regarding the CPA's competency in California tax law.

[4] The amended returns also indicated a California tax obligation for appellants, but as that return was not filed by this preparer, it is not relevant to the issue of whether the original preparer, who allegedly gave the erroneous advice, was competent in California tax law.

## HOLDING

Appellants have failed to show that the late filing of their 2016 return was due to reasonable cause and not willful neglect.

## DISPOSITION

Respondent's action denying appellants' claim for refund is sustained.

DocuSigned by:
Natasha Ralston
DE5900E5C6FD40F...
Natasha Ralston
Administrative Law Judge

We concur:

DocuSigned by:
John O Johnson
873D9797B9564E1...
John O. Johnson
Administrative Law Judge

DocuSigned by:
F8E81562726F448...
Richard Tay
Administrative Law Judge

Date Issued: 5/5/2021