OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

In the Matter of the Appeal of:	) OTA Case No. 18011296
J. GALLO	)
	)
	)
	)
	)

OPINION

Representing the Parties:

For Appellant: J. Gallo[1]

For Respondent: David Kowalczyk, Tax Counsel

A. LONG, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19045, J. Gallo (appellant) appeals an action by the Franchise Tax Board (respondent) proposing additional tax of $11,726.00, a demand penalty of $12,313.25, a late filing penalty of $2,931.50, a filing enforcement fee of $79.00, and applicable interest, for the 2014 tax year.[2]

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

ISSUES

1. Whether the Office of Tax Appeals (OTA) may order respondent to immediately refund any portions of additional tax when respondent has conceded that appellant is entitled to a partial refund during the pendency of an appeal.
2. Whether appellant has established reasonable cause for failing to timely reply to the Demand for Tax Return (Demand) for the 2014 tax year.
3. Whether appellant is entitled to the abatement of the filing enforcement fee.

[1] Grace Power from the Tax Assistance Appeals Program filed appellant's opening brief.

[2] On appeal, respondent concedes to abate the additional tax of $11,726 and to correspondingly reduce the demand penalty to $8,096. Additionally, respondent concedes to abate the late filing penalty.

FACTUAL FINDINGS

1. Appellant did not file a California income tax return for the 2014 tax year. Consequently, respondent sent appellant a Demand, stating that it had no record of receiving appellant's 2014 return. Respondent determined that appellant received enough income to require a tax filing after receiving information listed on Forms W-2 and 1099 issued to appellant by various entities. The Demand required appellant to file a 2014 return, provide evidence that a 2014 return was already filed, or explain why a 2014 return need not be filed. Relevant to this appeal, respondent had previously issued the following Demands and Notices of Proposed Assessment (NPAs) for previous tax years:

Tax Year	Demand Date	NPA Date
2010	1/25/2012	5/29/2012
2012	1/30/2014	5/19/2014
2013	5/05/2015	8/31/2015

2. After receiving no response to the 2014 Demand by the deadline, respondent issued an NPA. The NPA estimated appellant's income to be $512,495.60 and, after applying withholding credits, proposed a tax liability of $11,726.00. The NPA also imposed, among other things, a demand penalty of $12,313.25 and a filing enforcement fee of $79.00.
3. Appellant protested the NPA but respondent affirmed the NPA in a Notice of Action.
4. Subsequently, appellant filed a 2013 tax return and reported an overpayment of $51,912. Appellant requested that the overpayment be credited to the 2014 account as an estimated tax payment, and respondent has held the payment in suspense. Respondent notes that appellant has an additional credit from a $650 tax payment for 2014, which is also being held in suspense.
5. This timely appeal followed. On appeal, appellant submitted a 2014 joint California resident tax return and IRS Schedule D.[3] Respondent accepted the return as filed and reduced the amounts at issue in this appeal.

[3] Appellant's spouse is not a party to this appeal.

DISCUSSION

Issue 1: Whether OTA may order respondent to immediately refund any portions of additional tax when respondent has conceded that appellant is entitled to a partial refund during the pendency of an appeal.

Appellant seeks OTA to order respondent to immediately refund appellant's payments that are currently being held in suspense during the pendency of this appeal. OTA was established on July 1, 2017, by the Taxpayer Transparency and Fairness Act of 2017 to conduct appeals hearings for various taxes and fees administered by the California Department of Tax and Fee Administration and respondent. The basis of OTA's jurisdiction is set forth in statute. OTA does not have jurisdiction to address procedural issues, such as the propriety of respondent's collection actions. (See *Appeals of Wesley, et al.*, (2005-SBE-002) 2005 WL 3106917.) Our only power "is to determine the correct amount of an appellant's California personal income tax liability for the appeal years." (*Appeals of Dauberger, et al.*, (82-SBE-082) 1982 WL 11759.) Accordingly, we do not have jurisdiction to order respondent in regard to collection matters.

Issue 2: Whether appellant has established reasonable cause for failing to timely reply to the Demand for the 2014 tax year.

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. Respondent will only impose a demand penalty if: (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 for Tax Return or a Demand. (Cal. Code Regs., tit. 18, § 19133(b).) Here, based on appellant's failure to respond to prior Demands pursuant to California Code of Regulation, title 18, section 19133, respondent properly imposed the demand penalty for the 2014 tax year.

To establish reasonable cause, the taxpayer must show that the failure to timely respond to a Demand occurred despite the exercise of ordinary business care. (*Appeal of Bieneman* (82-SBE-148) 1982 WL 11825.) The taxpayer's reason for failing to respond to the Demand must be such that an ordinarily intelligent and prudent businessperson would have acted similarly under the circumstances. (*Appeal of Findley* (86-SBE-091) 1986 WL 22761.)

Appellant argues that the options presented in the Demand – file a return, provide proof that a return was already filed, or explain why appellant was not required to file a return – did not adequately describe appellant's situation. Appellant contends that she would owe no tax for the 2014 tax year once the credit from 2013 was applied to the 2014 account. Appellant also argues that she had four years to file a tax return under the statute of limitations to claim access to the credit. Finally, appellant argues that because respondent has conceded to removing the additional tax and reducing the demand penalty in its assessment, the NPA should now be void.

These reasons do not justify appellant's failure to respond to the Demand. No matter which option in the Demand appellant chose, appellant must, at a minimum, timely respond to the Demand in some form. Instead, appellant committed to inaction. A credit from a prior account year that could have been applied to the 2014 tax year would nonetheless require a tax filing in order to show that no additional tax was due.[4] The demand penalty is designed to penalize the taxpayer's failure to respond to a notice and demand, and not a taxpayer's failure to pay the proper tax. (*Appeal of Bryant* (83-SBE-180) 1983 WL 961596; *Appeal of Hublou* (77-SBE-102) 1977 WL 4093.)

Regarding the statute of limitations, appellant incorrectly states the law. Appellant argues that she had four years to file a return and that the law does not specify a due date to file a tax return. The Revenue and Taxation Code requires returns based on a calendar year to "be filed on or before the 15th day of April following the close of the calendar year." (R&TC, § 18566.) There is nothing in the law that states a taxpayer may file a return within four years without penalty. More importantly, the fact that appellant ultimately filed a 2014 return is not at issue, the demand penalty is imposed based upon appellant's failure to respond to the Demand.

Finally, respondent's concessions to reduce its assessment of additional tax and penalties does not invalidate the entire NPA. Every individual subject to the Personal Income Tax Law must make and file a return with respondent "stating specifically the items of the individual's gross income from all sources and the deductions and credits allowable" in excess of certain filing thresholds. (R&TC, § 18501(a)(1)-(4).) R&TC section 19087(a) provides that if any taxpayer fails to file a return, respondent at any time "may make an estimate of the net income, from any available information, and may propose to assess the amount of tax, interest, and

[4] When respondent issued the 2014 Demand, appellant had not yet filed a 2013 return to indicate that an overpayment would be available for the 2014 tax year.

penalties due." When respondent makes a proposed assessment of additional tax based on an estimate of income, respondent's initial burden is to show that its proposed assessment is reasonable and rational. (*Todd v. McColgan* (1949) 89 Cal.App.2d 509, 514; *Appeal of Bindley*, 2019-OTA-179P.) When a taxpayer fails to file a valid return, respondent's use of income information from various sources to estimate a taxpayer's taxable income is a reasonable and rational method of estimating taxable income. (See *Palmer v. Internal Revenue Service* (9th Cir. 1997) 116 F.3d 1309, 1313.) Once respondent has met its initial burden, the assessment is presumed correct, and the taxpayer has the burden of proving otherwise. (*Todd v. McColgan*, *supra*.)

Here, once appellant filed a 2014 return, respondent accepted the return and accordingly reduced the 2014 assessment. We find no basis in the law to invalidate a proposed nor corrected assessment, so long as there is a reasonable and rational basis for the remaining assessment. Moreover, any error in the proposed assessment appears to have arisen from appellant's failure to timely make and file a return. "[A] taxpayer is not in a good position to criticize respondent's estimate of his or her liability when he or she fails to file a required return and, in addition, subsequently refuses to submit information upon request." (*Appeals of Dauberger, et al.*, *supra*.)

Issue 3: Whether appellant is entitled to the abatement of the filing enforcement fee.

R&TC section 19254(a)(2) requires respondent to impose a filing enforcement fee if a taxpayer fails to file a return within 25 days after respondent mails a demand letter to the taxpayer. Once the fee is properly imposed, the fee cannot be abated under any circumstances including for reasonable cause. (*Appeal of GEF Operating, Inc.*, 2020-OTA-057P.) Here, respondent mailed the Demand on April 19, 2017, and appellant did not file a return within 25 days of its mailing. Accordingly, respondent properly imposed the filing enforcement fee and we have no legal authority for abating it.

HOLDINGS

1. OTA does not have the power to order respondent to immediately refund any portions of additional tax when respondent has conceded that appellant is entitled to a partial refund during the pendency of an appeal.

2. Appellant has not established reasonable cause for failing to timely reply to the Demand for the 2014 tax year.
3. Appellant is not entitled to the abatement of the filing enforcement fee.

DISPOSITION

Respondent's action is modified in accordance with its concession on appeal to abate the proposed tax and late filing penalty, and reduce the demand penalty and interest accordingly. Respondent's action is otherwise sustained.

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Andrea L.H. Long
Administrative Law Judge

We concur:

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Elliott Scott Ewing
Administrative Law Judge

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John O. Johnson
Administrative Law Judge

Date Issued: 1/6/2021