

**OFFICE OF TAX APPEALS
STATE OF CALIFORNIA**

In the Matter of the Appeal of:

J. BELCHER) OTA Case No. 19105326
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)**OPINION**

Representing the Parties:

For Appellant:

Nikki L. McLaughlin, TAAP¹
Mengun He, Supervising Attorney

For Respondent:

Phillip Kleam, Tax Counsel III
Nancy Parker, Tax Counsel IV

A. ROSAS, Administrative Law Judge: Under Revenue and Taxation Code (R&TC) section 19324, appellant J. Belcher appeals respondent Franchise Tax Board's action in denying appellant's claim for refund for tax year 2017. The claim for refund consists of a late-filing penalty of \$8,218.25, plus interest of \$1,594.19.

Office of Tax Appeals Administrative Law Judges Amanda Vassigh, Elliott Scott Ewing, and Alberto T. Rosas held an oral hearing for this matter on December 15, 2020.² At the conclusion of the hearing, the record was closed and this matter was submitted for decision.

ISSUES

1. Whether appellant's failure to timely file a tax return for tax year 2017 was due to reasonable cause.
2. Whether appellant is entitled to interest abatement.

¹ Ms. McLaughlin is a law student with the Tax Appeals Assistance Program.

² The oral hearing was noticed for Sacramento, California and conducted electronically due to COVID-19.

FACTUAL FINDINGS

Background & Mental Health

1. In December 2016, when appellant was in her early 70s, she underwent knee replacement surgery. It took appellant approximately six months to recover. She was mostly on bed rest through March 2017, and she was in pain until approximately June 2017.
2. Appellant felt depressed after her knee surgery and recovery. Between April 2017 through May 2018, appellant had about 30 sessions with a psychotherapist, whom we will refer to as Dr. MH. Appellant had two sessions with Dr. MH in April 2018 and another two sessions in May 2018.
3. In 2018, appellant was enrolled in undergraduate courses on at least a half-time basis. Then, in the fall of 2018, she enrolled in graduate courses on at least a half-time basis.
4. In November 2018, appellant was diagnosed with Major Depressive Disorder (MDD).³
5. At around this time, during the fall of 2018, appellant contacted a Certified Public Accountant (CPA) to help with her taxes for tax year 2017.
6. Since November 2018, appellant consistently participated in a mental health program called “Restoring Emotional and Cognitive Health” as part of her recommended treatment for depression.
7. In November 2018, appellant started seeing a new psychiatrist, whom we will refer to as Dr. PG. Through February 2020, they had 52 individual psychotherapy sessions.

Tax Year 2017

8. Appellant filed an untimely 2017 California Resident Income Tax Return on March 2, 2019. Appellant reported that she sold a parcel of real property on June 16, 2017. She reported rental income from four properties: two single-family residences rented all year and two short-term vacation rentals. Appellant reported a tax balance due of \$32,873.

³ While health issues are generally a matter of private concern, we discuss appellant’s MDD because her mental health forms the basis of her argument. But out of respect for appellant’s privacy, we discuss only those facts that we believe are relevant to our analysis and conclusion. If there are facts related to appellant’s mental health that we do not discuss, it is not because we disbelieve such facts, but because such facts would not have affected our analysis or conclusion.

9. After accepting and processing the tax return, respondent imposed a late-filing penalty of \$8,218.25. Respondent issued a Notice of Tax Return Change – Revised Balance for the balance of \$42,686.18, which included the tax balance due, the late-filing penalty, and interest of \$1,594.93. This notice required payment in full by March 26, 2019.
10. In March 2019, appellant submitted three payments to respondent, all of them by the deadline stated in the notice. The three payments resulted in a slight overpayment, which respondent refunded to appellant.
11. Appellant submitted a letter dated March 28, 2019, requesting abatement of the late-filing penalty of \$8,218.25 and interest of \$1,594.19. On July 8, 2019, respondent denied the claim for refund, and this timely appeal followed.

DISCUSSION

Issue 1 - Whether appellant's failure to timely file a tax return for tax year 2017 was due to reasonable cause.

Because appellant failed to timely file the 2017 California tax return by April 15, 2018, or by the automatic six-month extension, respondent imposed a late-filing penalty of \$8,218.25. Respondent imposes a late-filing penalty when a taxpayer does not timely file a return, unless it is shown that the failure to timely file was due to reasonable cause and not due to willful neglect. (R&TC, § 19131(a).) When respondent imposes this penalty, the law presumes that it is correct. (*Appeal of Xie*, 2018-OTA-076P.) A taxpayer has the burden of establishing reasonable cause. (*Appeal of Scott* (82-SBE-249) 1982 WL 11906 (*Scott*).) The applicable standard of proof is by a preponderance of the evidence. (Cal. Code Regs., tit. 18, § 30219(c).)

To meet this evidentiary standard, a party must establish by documentation or other evidence that the circumstances it asserts are more likely than not to be correct. (*Concrete Pipe and Products of California, Inc. v. Construction Laborers Pension Trust for Southern California* (1993) 508 U.S. 602, 622 (*Concrete Pipe*).) In other words, the preponderance of the evidence standard means more than 50 percent. (*Union Pacific Railroad Co. v. State Bd. of Equalization* (1991) 231 Cal.App.3d 983, 1000.) Taxpayers must provide credible and competent evidence to support the claim of reasonable cause; otherwise, the penalty will not be abated. (*Appeal of Walshe* (75-SBE-073) 1975 WL 3557.)

As a result of appellant's extensive evidence on the subject of MDD in general, we understand the common symptoms of MDD and that "severe mental illnesses" include MDD. We understand that persons suffering from MDD may not choose to willfully neglect their responsibilities. In this appeal, there are no allegations of willful neglect, and appellant does not dispute the late-filing penalty computation. Thus, our focus is on reasonable cause.

For a taxpayer to establish that a failure to act was due to reasonable cause, the taxpayer must show that the failure occurred despite the exercise of ordinary business care and prudence, or that cause existed as would prompt an ordinarily intelligent and prudent businessperson to have so acted under similar circumstances. (*Appeal of Bieneman* (82-SBE-148) 1982 WL 11825.) Illness or other personal difficulties may be considered reasonable cause, if taxpayers present credible and competent proof that they were continuously prevented from filing a tax return. (*Appeal of Head and Feliciano*, 2020-OTA-127P (*Head & Feliciano*); *Appeal of Halaburka* (85-SBE-025) 1985 WL 15809 (*Halaburka*.) When taxpayers allege reasonable cause based on an incapacity due to illness, the duration of the incapacity must approximate that of the tax obligation deadline. (*Head & Feliciano, supra*; see *Wright v. Commissioner*, T.C. Memo. 1998-224, citing *Hayes v. Commissioner*, T.C. Memo. 1967-80.) However, if the difficulties simply caused the taxpayers to sacrifice the timeliness of one aspect of their affairs to pursue other aspects, the taxpayers must bear the consequences of that choice. (*Head & Feliciano, supra*; *Appeal of Orr* (68-SBE-010) 1968 WL 1640.)

Appellant argues that her mental illness constituted reasonable cause for her failure to timely file a tax return for tax year 2017. In December 2016, appellant underwent knee replacement surgery. She felt depressed after her surgery and recovery. From April 2017 through May 2018, appellant had about 30 sessions with Dr. MH, a psychotherapist. Then, in November 2018, appellant was diagnosed with a severe mental illness known as MDD. Appellant argued at the oral hearing that her failure to file in a timely manner was the direct result of her knee replacement surgery followed by her subsequent MDD diagnosis.

Mental illness or mental incapacity can constitute reasonable cause for the failure to file timely returns. (*Williams v. Commissioner* (1951) 16 T.C. 893, 906; *Wilkinson v. Commissioner*, T.C. Memo. 1997-410 (*Wilkinson*); and see *Carlson v. United States* (7th Cir.1997) 126 F.3d 915, 922 (*Carlson*) [addressing reasonable cause exception with respect to failure to pay].) But the taxpayer must show that the "mental or emotional disorder . . . rendered the taxpayer

incapable of exercising ordinary business care and prudence during the period in which the failure to file continued.” (*Wilkinson, supra.*)

The current case law upon which we must rely considers reasonable cause due to mental illness only in cases where taxpayers have been severely restricted from meeting their tax obligations. For instance, the U.S. Tax Court found reasonable cause in a case where the taxpayer was confined to hospitals for severe mental illness. (*Carnahan v. Commissioner*, T.C. Memo. 1994 -163, *affd.* without published opinion (D.C. Cir. 1995) 70 F. 3d. 637.) However, in a case in which a taxpayer suffered from severe major depression and other disorders, the U.S. Tax Court did not “see enough evidence of her inability to manage her other business affairs” during the time in question, despite her difficulty doing so. (*Leslie v. Commissioner*, T.C. Memo. 2016-171.) The court acknowledged “the standard is a tough one to meet ... but because she was still able to live on [rental property] income we find that her ability to ‘carry on normal activities’ was not so impaired as to be an inability.” (*Ibid.*, citing *Wilkinson, supra.*) In other words, if the taxpayer is able to exercise ordinary care and prudence with respect to nontax matters, the claimed mental illness or mental incapacity does not constitute reasonable cause. (See *Carlson, supra*, at p. 923.)

Because appellant failed to timely file the 2017 California tax return by April 15, 2018, or by the automatic six-month extension, we are principally concerned with this six-month period from April 15, 2018, through October 15, 2018. But to fully understand and appreciate the facts in this case, and to fully analyze appellant’s claimed mental incapacity from MDD, we examine the nontax matters following her knee replacement surgery in December 2016.

It took appellant approximately six months to recover from her knee replacement surgery. She was mostly on bed rest through March 2017, and she was in pain until approximately June 2017. At around this time, on June 16, 2017, appellant sold a parcel of real property. Although this sale occurred at the tail end of her recovery period, appellant testified that her Realtor “basically did everything” and “handled it all.” In the year following her surgery, appellant received rental income from four properties: two single-family residences rented all year and two short-term vacation rentals. Appellant explained that the rental income was passive and her involvement with these properties was minimal.

Since her MDD diagnosis in November 2018, appellant consistently participated in “Restoring Emotional and Cognitive Health,” a mental health program as part of her

recommended treatment for depression. As mentioned above, she also started seeing a new psychiatrist, Dr. PG, in November 2018. There is a gap between appellant's last visit with Dr. MH in May 2018 and her diagnosis in November 2018. Appellant argued that she was not diagnosed with MDD earlier because of delays with the hospital's internal administrative processes. Appellant argued that these delays prevented her from receiving a full assessment sooner, thus delaying her access to the hospital's mental health services until the fall of 2018.

Appellant's evidence provided background and context about legal problems faced by the hospital as a result of its overall administrative delays. Appellant asks us to infer that but for the hospital's administrative delays, she would have been diagnosed with MDD much sooner. However, "an inference is not evidence but rather the result of reasoning from evidence." (*Fashion 21 v. Coalition for Humane Immigrant Rights of Los Angeles* (2004) 117 Cal.App.4th 1138, 1149 (*Fashion 21*)). And based on the evidence, it is not clear when appellant first contacted the hospital to seek treatment or a diagnosis for her mental health.

Between April 2017 through May 2018, appellant had about 30 sessions with a psychotherapist, Dr. MH. Although appellant explained that she felt depressed after her knee surgery and recovery, the evidence does not include any clinical summaries signed by Dr. MH, who saw appellant during part of the six-month period of our focus, specifically seeing appellant twice in April 2018 and twice more in May 2018. We know nothing about Dr. MH's treatment or diagnosis of appellant.⁴

Even if we accepted the inference that but for the hospital's administrative delays, appellant would have been diagnosed with MDD by April 15, 2018, such inference does not explain appellant's active participation in nontax matters. When a taxpayer is able to exercise ordinary care and prudence with respect to nontax matters, the claimed mental illness or mental incapacity does not constitute reasonable cause. (See *Carlson, supra*, at p. 923.) Some of the more revealing nontax matters from 2018 concern appellant's enrollment in college courses. In 2018, while in her early 70s, appellant was enrolled in undergraduate courses on at least a half-time basis. Then, in the fall of 2018, appellant enrolled in graduate courses on at least a half-time basis. These facts weigh against appellant's ability to prove that her MDD "rendered [her]

⁴ In contrast, appellant submitted a great deal of evidence about the treatment she received from her new psychiatrist, Dr. PG, whom she started seeing in November 2018. The evidence indicates that between November 2018 through February 2020, appellant had 52 individual psychotherapy sessions with Dr. PG and saw much improvement as a result of these sessions. The evidence includes a detailed clinical summary signed by Dr. PG.

incapable of exercising ordinary business care and prudence during the period in which the failure to file continued.” (*Wilkinson, supra.*)

In addition, at around this time, during the fall of 2018, appellant contacted a CPA to help with her taxes for tax year 2017, but appellant provided no reason or evidence to explain why appellant did not, or could not, contact this CPA sooner. To satisfy her burden of proof, appellant must present credible and competent proof that she was continuously prevented from filing a tax return. (*Head & Feliciano, supra; Halaburka, supra.*) The duration of the incapacity must approximate that of the tax obligation deadline. (*Head & Feliciano, supra.*) Thus, we are principally concerned with the six-month period from April 15, 2018, through October 15, 2018.

During the oral hearing, appellant was asked to focus her testimony on this six-month period. Appellant did not provide any specificity; instead, appellant testified that she “was depressed” during this six-month period, “and the thing is in depression you go in and out. Sometimes you’re just fine.” Rather than focus on this six-month period, appellant discussed things that took place starting in November 2018, after she had already failed to timely file her tax return by the automatic six-month extension. For example, during her testimony, she discussed that in November 2018 she started participating in a mental health program and started seeing Dr. PG.

Based on the evidence, we know about appellant’s knee replacement surgery in December 2016. We know a great deal about her health diagnosis and treatment starting in November 2018. But we know very little about the six-month period from April 15, 2018, to October 15, 2018. We know she saw Dr. MH twice in April and twice in May. We know that before the fall semester in 2018, she was enrolled in undergraduate courses on at least a half-time basis, and that in the fall semester she enrolled in graduate courses on at least a half-time basis.

As we explained, a taxpayer has the burden of establishing reasonable cause. (*Scott, supra.*) A party must establish by documentation or other evidence that the circumstances it asserts are more likely than not to be correct. (*Concrete Pipe, supra*, at p. 622.) Based on the lack of evidence about the specific six-month period, we conclude that appellant did not prove that she was continuously prevented from filing a tax return from April 15, 2018, to October 15, 2018. Moreover, based on her enrollment in undergraduate and graduate courses in 2018, appellant failed to prove that her MDD “rendered [her] incapable of exercising ordinary

business care and prudence during the period in which the failure to file continued.” (*Wilkinson, supra.*)

The case law sets a tough standard for establishing reasonable cause based on mental illness, and the facts in this case left us with a difficult decision. We understand that appellant’s depression was “in and out” during this six-month period, but because she was able to exercise ordinary care and prudence from April 15, 2018, to October 15, 2018, with respect to nontax matters, we conclude that the claimed mental illness or mental incapacity does not constitute reasonable cause. Rather, based on the evidence, it seems that the difficulties due to MDD caused appellant to sacrifice the timeliness of one aspect of her affairs to pursue other aspects. Due to the tough standard for establishing reasonable cause, we must conclude that appellant did not meet her burden of establishing that the late filing was due to reasonable cause.

Lastly, we turn to appellant’s argument that the Internal Revenue Service (IRS) abated her federal penalties due to reasonable cause. The evidence included excerpts from the IRS’s procedural manuals, as well as the IRS’s Individual Master File (IMF) transcript for appellant for tax year 2017. Appellant asks us to draw a specific inference from the penalty reason code used on the IMF transcript, arguing that the use of code 062 shows that the IRS abated appellant’s penalties due to reasonable cause. Respondent argues, however, that the IRS uses code 062 in combination with code 020 for first-time abatement. Here, it is not clear whether the IRS abated appellant’s federal penalties due to reasonable cause or due to the first-time abatement program.⁵ Appellant did not provide IRS documentation that states that the IRS abated the same penalty for reasonable cause. Instead, appellant makes references to a code on the IMF transcript, attempts to decipher what the code means, and argues that code 062 means we should infer that the IRS abated the penalties due to reasonable cause. As mentioned above, however, “an inference is not evidence” (*Fashion 21, supra*, at p. 1149.) “ ‘It must be such that a rational, well-constructed mind can reasonably draw from it the conclusion that the fact exists[.]’ ” (*Ibid.*, quoting *Wigodsky v. Southern Pac. Co.* (1969) 270 Cal.App.2d 51, 55.) Here, based on the evidence and the use of code 062 on the IMF transcript, we cannot reasonably draw the conclusion that the IRS abated appellant’s penalties due to reasonable cause.

Thus, the late-filing penalty will not be abated.

⁵ California does not conform to federal relief from penalties based upon good filing history or first-time abatement. However, respondent may abate a penalty if a taxpayer can provide IRS documentation clearly stating that the IRS abated the same penalty for “reasonable cause.”

Issue 2 – Whether appellant is entitled to interest abatement.

The interest amount at issue is \$1,594.19. Imposing interest is mandatory, and respondent cannot abate interest except where authorized by law. (R&TC, § 19101(a); *Appeal of Balch*, 2018-OTA-159P.) Interest is not a penalty; it is compensation for the use of money. (*Ibid.*) There is no reasonable cause exception to the imposition of interest. (*Appeal of Gorin*, 2020-OTA-018P.) Generally, to obtain relief from interest, taxpayers must qualify under R&TC sections 19104, 19112, or 21012. Other than appellant’s main argument that she had reasonable cause for untimely filing a tax return, appellant does not specify why she may be entitled to interest abatement. Appellant does not allege that any of the three statutory provisions for interest abatement apply to the facts of this case; and based on the arguments presented and the evidence in the record, we conclude that none of these statutory provisions apply. Therefore, appellant did not show that she is entitled to interest abatement.

HOLDINGS

1. Appellant did not show that the failure to timely file her tax return for tax year 2017 was due to reasonable cause.
2. Appellant did not show that she is entitled to interest abatement.

DISPOSITION

We sustain respondent’s denial of appellant’s claim for refund.

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Alberto T. Rosas
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Alberto T. Rosas
Administrative Law Judge

We concur:

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Amanda Vassigh
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Amanda Vassigh
Administrative Law Judge

DocuSigned by:
E.S. Ewing
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Elliott Scott Ewing
Administrative Law Judge

Date Issued: 3/18/2021