



BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
PRIME COMPUTER, INC.)

For Appellant: George L. **Connor**, Jr.
Tax Specialist

For Respondent: James T. **Philbin**
Supervising Counsel

O P I N I O N

This appeal is made pursuant to section 26075, subdivision (a), of the Revenue and Taxation Code from the action of the Franchise **Tax** Board in denying the claim of Prime Computer, Inc., for refund of penalties in the amount of **\$2,413.04** for the income year 1979.

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Appellant, a Delaware corporation engaged in the business of manufacturing and selling computers, files its California franchise tax returns on a calendar year basis. For the year 1979, appellant requested and received an extension of time in which to file its franchise tax return. The request for an extension indicated an expected tax liability of \$200. The return was ultimately filed on September 15, 1980, which was within the extension period. The **return**, which reflected a liability of \$41,147, was accompanied by a payment of **\$29,547**.

Respondent's review of **appellant's** account disclosed that its estimated tax payments in 1979 had been made in the following manner:

	<u>Date Paid</u>	<u>Amount</u>	<u>Cumulative</u>
1st Installment	3/15/79	\$2,250	\$ 2,250
2nd Installment	6/15/79	2,250	4,500
3rd Installment	9/15/79	4,200	8,700
4th Installment	12/26/79	2,900	11,600

On the basis of 'the above schedule, respondent determined that appellant was subject to penalties in the total amounts of **\$2,367.10**, consisting of **\$1,367.10** for underpayment of estimated tax (Rev. & Tax. Code, § 25951) and **\$1,000 for late payment of tax** (Rev. & Tax. Code, § 25934.2). Appellant paid these amounts, together with \$45.94 in accrued interest, and filed a claim for refund. Respondent's denial of that claim led to this appeal.

Appellant argues **here that** respondent's assessment of the penalty for underpayment of estimated tax (Rev. & Tax. Code, § 25951) is in error because its estimated payments made in 1979 complied with the exception contained in subdivision (a) of section 25954 of the Revenue and Taxation Code,^{1/} Appellant further contends that the penalty for late payment (Rev. & Tax. Code, § 25934.2) is also in error because there was reasonable cause to excuse such late payment within the meaning of section 25934.2, subdivision (a). We hold, however, that respondent has properly assessed both penalties.

A penalty for underpayment of estimated tax is imposed by section 25951, which states:

^{1/} All statutory references are to the Revenue and Taxation Code, unless otherwise noted.

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In case of any underpayment of estimated tax, except as provided in Section 25954, there shall be added to the tax for the taxable year an amount determined at the rate of 12 percent per annum upon the amount of underpayment (determined under Section 25952) for the period of the underpayment (determined under Section 25953).

Under section 25952 there is no "underpayment" of estimated tax if the taxpayer has paid 80 percent of each installment otherwise due on each of the prescribed dates. Thus, if appellant had made four timely estimated tax payments, each in the amount of at least **\$8,229.40** (80% x (25% x **\$41,147**)), there would have been no underpayment. As indicated above, however, none of appellant's prepayments of tax in 1975 exceeded \$4,200.

The "period of the underpayment" runs from the installment due date to the date of payment or the return filing date, whichever is earlier. (Rev. & Tax. Code, § 25953.) No amount of any prepayment will be applied to any previous underpayment of estimated tax, except to the extent such payment exceeds 80 percent of the installment then due.^{2/} (Rev. & Tax. Code, § 25953, subd. (b).) Under these provisions, respondent correctly determined the periods of underpayment of appellant's estimated tax.

It therefore appears that this penalty was properly computed and assessed, unless appellant qualifies for relief under section 25954. That section provides, in substance, that no penalty will be imposed if the total amount of estimated tax **payments made** by each installment due date equals or exceeds the amount that would have been due by such date if the estimated tax were the lesser of:

(a) the tax shown on the taxpayer's return for the preceding income year;

(b) the tax computed at the rates for the current taxable year but otherwise on the basis of the facts and law applicable to the return for the preceding taxable year; or

^{2/} **Note** that the "installment then due" is the amount **determined** under subdivision (a) of section 25952 based upon the actual tax liability shown on the return for the income year, not that of the preceding income year.

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(c) for income years beginning after December **31, 1971**, an amount equal to 80 percent of the **tax** for the taxable year computed by placing on an annualized basis the taxable income for stated periods of the income year preceding each estimated tax installment due date.

Appellant contends that it qualifies **for** relief from the penalty assessment under subdivision (a) above. In order for subdivision (a) of section 25954 to apply, it must be determined that the estimated payments made during each installment period equaled or exceeded the amount which would have been due by the end of **each** installment period if the estimated tax were that shown on the taxpayer's return for the preceding income year. 'In the instant case, the tax shown on appellant's return for the income year 1978 was \$11,463. Under the subdivision (a) exception, the amount of estimated tax due on or before the end of each installment period was therefore **\$2,292.60** and the cumulative amounts due by the respective installment dates were **\$2,292.60, \$4,585.20, \$6,877.80** and **\$9,170.40**. As can be seen, only appellant's estimated tax payment of \$4,200 on September 15, 1979, meets the penalty relief requirement of subdivision (a) of section 25954, and respondent properly determined that no penalty applied for that installment period. Thus, appellant did not meet the penalty relief requirement for any other installment.

On the record before us, subdivision (a) of section 25954 is the only exception which could be applied in this case. Since we have found that appellant failed to meet its provisions, except for the third installment, we must conclude that the penalty for underpayment of the first, second and fourth installments of estimated tax, as computed by respondent, was properly assessed against appellant for its income year **1979**.

As indicated above, respondent also assessed a \$1,000 penalty for the late payment of the tax. Appellant challenges the imposition of this penalty arguing that the late payment was due to an audit by respondent of the years 1975 through 1977, which was not settled until March 15, 1980. Appellant alleges that this audit necessitated a change to the unitary method of reporting income and the difficulties of estimating such tax then due constituted reasonable cause for the late payment.

Section'25934.2 provides, in pertinent part:

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(a) If any taxpayer fails to pay the amount of tax required to be paid under Sections 25551 and 25553 by the date prescribed therein, then unless it is shown that the failure was due to reasonable cause and not willful neglect, a penalty of 5 percent of the total tax unpaid as of the date prescribed in Sections 25551 and 25553 shall be due and payable upon notice and demand from the Franchise Tax Board. ... In no case, however, may the penalty imposed under this section be less than five dollars (\$5) or more than one thousand dollars (\$1,000).

Section 25551, which is applicable to appellant, provides:

Except as otherwise provided in this chapter, the tax imposed by this part shall be paid not later than the time fixed for filing the return (determined without regard to any extension of time for filing the return).
(Emphasis added.)

The normal due date for filing appellant's return for the calendar year 1979 was March 15, 1980. (Rev. & Tax. Code, § 25401, subd. (a).) Since appellant failed to pay \$29,547 of its total franchise tax liability for that year until September 15, 1980, respondent's imposition of the penalty for late payment of tax was proper, unless such untimely payment was due to reasonable cause and not due to willful neglect. Appellant bears the burden of proving that both of those conditions existed. (Rogers Hornsby, 26 B.T.A. 591 (1932); see Appeal of Telonic Altair, Inc., Cal. St. Bd. of Equal., May 4, 1978.) In order to establish reasonable cause, the taxpayer must show that its failure to act occurred despite the exercise of ordinary business care and prudence.^{3/} (See Sanders v. Commissioner, 225 F.2d 629 (10th Cir. 1955), cert. den., 350 U.S. 967 [100 L.Ed. 839] (1956); Appeal of Citicorp Leasing, Inc., Cal. St. Bd. of Equal., Jan. 6, 1976.) In addition, the regulation interpreting section 25934.2 provides that in order to avoid the penalty, a taxpayer "must make an affirmative showing of

^{3/} Since appellant did not pay 90 percent of the tax shown on the return by the due date, the presumption of reasonable cause provided by regulation is inapplicable. (Former Cal. Admin. Code, tit. 18, reg. 25934.2 (repealer filed Nov. 29, 1982; Register 82, No. 49).)

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all facts alleged as reasonable cause for his failure to pay such tax in the form of a written statement." (Former Cal. Admin. Code, tit. 18, reg. 25934.2, subd. (a.) (repealer filed Nov. 29, 1982; Register 82, No. 49).)

We find that appellant has not made such "an affirmative showing of all the facts" as would fulfill its burden of proving reasonable cause.. Appellant has merely stated that an audit completed on March 15, 1980, resulted in requiring a change to the unitary basis for reporting its income. From the record before us, we are unable to see what difficulties resulted from the audit, when they arose, and what relationship they may have had to the late payment of tax. Accordingly, we have no choice but to conclude that respondent's imposition of this penalty must be sustained. Moreover, we note that we have held that the difficulty resulting from resolving certain accounting problems arising from federal law does not constitute reasonable cause for late payment of tax. (Appeal of Cerwin-Vega International, Cal. St. Bd. of Equal., Aug. 15, 1978.) Appellant's contention here would appear to be but a variation of this rejected argument.

For the reasons cited above, respondent's action in this matter must be sustained.

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O R D E R

Pursuant to the views expressed in the opinion of the board on file in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to section 26077 of the Revenue and Taxation Code, **that the** action of the Franchise Tax Board in **denying the** claim of Prime Computer, Inc., **for** refund Of **penalties** in the amount of **\$2,413.04** for the income year **1979**, be-and the same is hereby sustained.

Done at Sacramento, California, this 15th day of September , 1983, by the State Board of Equalization, with Board Members Mr. Bennett, **Mr. Collis**, **Mr. Dronenburg**, **Mr. Nevins** and Mr. Harvey **present**.

William M. B e -- - , Chairman
Conway H. Collis , Member
Ernest J. Dronenburg, Jr. , Member
Richard Nevins , Member
Walter Harvey* , Member

*For Kenneth Cory, per Government Code section 7.9