OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

In the Matter of the Appeal of:	) OTA Case No. 20086555
DIGITAL MARKETING STRATEGY	)
	)
	)
	)

OPINION

Representing the Parties:

For Appellant: Bryan R. Nuxoll, TAAP[1]
Mengjun He, TAAP

For Respondent: Christopher Tuttle, Tax Counsel,
Maria Brostherhous, Tax Counsel IV

N. RALSTON, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19324, Digital Marketing Strategy (appellant) appeals an action by the Franchise Tax Board (respondent) denying appellant's claim for refund of $958.16[2] for the 2018 tax year.

Office of Tax Appeals Administrative Law Judges Cheryl L. Akin, Sara A. Hosey, and Natasha Ralston held an oral hearing for this matter via Webex on December 17, 2021. At the conclusion of the hearing, the record was closed, and this matter was submitted for an opinion.

[1] TAAP stands for the Taxpayers Appeals Assistance Program (TAAP). Joshua Imeri-Garcia of TAAP represented appellant at the time this Opinion was issued. Bryan R. Nuxoll of TAAP represented appellant at the hearing. Brittany Cho of TAAP, filed appellant's Supplemental Brief. Michael Shaheen of TAAP filed appellant's Reply Brief. Appellant filed its own Opening Brief.

[2] This amount consists of $800 in tax, $114.90 in penalties and $43.26 in interest.

ISSUE[3]

1. Whether appellant is subject to the minimum franchise tax for taxable year ending December 31, 2018.
2. Whether appellant has established reasonable cause to abate the late payment penalty.
3. Whether appellant has established cause to abate the underpayment of estimated tax penalty.
4. Whether appellant has established that interest should be waived or abated.

FACTUAL FINDINGS

1. Appellant filed a timely California S Corporation Return for 2018, using a California address which was marked both as appellant's initial and final return. The return reported a California address for appellant, an incorporation date of December 13, 2017, a dissolution date of December 31, 2018, listed the state of incorporation as Texas, and indicated that appellant began doing business in California on December 1, 2018. Appellants did not report any franchise or income tax due on this return.
2. Subsequently, respondent sent appellant a Notice of Tax Return Change notifying appellant that respondent had assessed the minimum franchise tax of $800, an underpayment of estimated tax penalty (estimated tax penalty) of $30.90 and a late payment penalty of $84.00, plus interest.
3. Appellant submitted a payment of $958.16 on February 14, 2020, and subsequently filed a claim for refund.
4. Respondent denied appellant's claim for refund.
5. Appellant filed this timely appeal.
6. During the course of this appeal appellant provides an email it sent to its tax preparer asking the tax preparer to confirm her competency and advice to appellant. Specifically, the email asked the tax preparer to provide a letter indicating that: 1) the tax preparer has expertise in California tax law, 2) appellant fully disclosed all necessary and accurate information, 3) and the tax preparer advised appellant that there was no filing requirement. The tax preparer responded via email also dated December 9, 2020, stating

[3] At the prehearing conference, appellant stated that it will only be discussing the late payment penalty at the hearing but is not specifically conceding any other issue.

"I am unable to confirm items 2 and 3, but if there is another type of letter you would like us to prepare…".

DISCUSSION

Issue 1: Whether appellant is subject to the minimum franchise tax for taxable year ending December 31, 2018.

FTB's determination of tax is presumed to be correct, and a taxpayer has the burden of proving error. (*Appeal of GEF Operating, Inc*. 2020-OTA-057P.) Unsupported assertions are not sufficient to satisfy a taxpayer's burden of proof. (*Ibid*.) FTB's determinations cannot be successfully rebutted when the taxpayer fails to provide credible, competent, and relevant evidence as to the issues in dispute. (*Ibid*.)

R&TC section 23153(b)(3) provides that a corporation "doing business" in California is required to pay the annual minimum franchise tax. For the 2018 tax year, the amount of this tax was $800. (R&TC, § 23153(d)(1).) "Doing business" is defined as "actively engaging in any transaction for the purposes of financial or pecuniary gain or profit." (R&TC, §23101(a).) R&TC section 23153(f)(1) provides that a corporation that incorporates in California or registers with the Secretary of State is not subject to the annual tax for its first California tax year.

Appellant indicated on its 2018 return that it was "doing business" in California. However, appellant did not incorporate in California or register with the California Secretary of State. Appellant contends that the business failed and dissolved within its first year and that appellant was incorrectly advised by its accountant that it was exempt from the annual minimum tax. The fact that appellant indicated on its return that it was doing business in California is sufficient to find that appellant was actually doing business in California. Further, appellant did not dispute this fact and reports a California address for appellant on the 2018 return. As such, appellant is required to pay the annual minimum franchise tax because it was doing business in California. Furthermore, because appellant did not incorporate in California and did not register

with the California Secretary of State, appellant does not meet the requirements to be exempt from the minimum tax for the first year.

Issue 2: Whether appellant has established reasonable cause to abate the late payment penalty.

R&TC section 19132 imposes a late payment penalty when a taxpayer fails to pay the amount shown as due on the return by the date prescribed for the payment of the tax. Generally, the date prescribed for the payment of the tax is the due date of the return (without regard to extensions of time for filing). (R&TC, § 19001.) 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, § 19132(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.) 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. (*United States v. Boyle,* (1985) 469 U.S. 241, 250, *Appeal of Summit Hosting*, 2021-OTA-216P.)[4] By contrast, reliance on an expert cannot function as a substitute for compliance with an unambiguous statute. (*United States v. Boyle, supra,* 469 U.S. at p. 251.) 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.

Appellant does not contest whether the late payment penalty was properly imposed or computed. Rather, appellant asserts that reasonable cause exists to abate the penalty. Appellant contends that it has established reasonable cause because it relied on its tax preparer, who provided it with the erroneous advice that it was not required to pay the $800 minimum franchise tax for the 2018 tax year. Appellant's tax preparer also filed appellant's 2018 tax return

[4] 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.)

reporting no tax due, which appellant took as further evidence that it did not have a tax liability. Based on its tax preparer's advice, appellant contends that it failed to timely pay the $800 minimum franchise tax and thus, incurred a late payment penalty. Respondent contends that appellant failed to establish reasonable cause for abatement of the late payment penalty because appellant failed to demonstrate that the tax preparer was apprised of all relevant facts and documents at the time she filed appellant's tax return, that the preparer was competent in California tax law, and that appellant relied in good faith on the tax preparer's advice.

Appellant argues that its tax preparer was competent in California tax law and was apprised of all relevant facts and documents at the time that she filed appellant's tax return. Appellant further argues that it relied on the tax preparer's advice in good faith. To show that its tax preparer was competent in California tax law, appellant provides emails and letters from the tax preparer in which she lists her title as an Enrolled Agent, Senior Tax Accountant. Appellant also stated that its tax preparer had 20 years of experience, advised appellant for a fee, handled appellant's California tax matters, and also contacted respondent and the California Secretary of State on appellant's behalf in order to try to resolve the tax liability. Appellant further points out that the California Tax Education Counsel (CTEC) sets forth requirements that apply to anyone who prepares tax returns for a fee within the state of California and is not an exempt preparer. Appellant notes that Enrolled Agents are exempt from CTEC requirements, while Certified Public Accountants (CPA) must comply with the CTEC requirements. Thus, appellant concludes that the state of California has determined that Enrolled Agents are competent in California tax law. Appellant also points out that its tax preparer did not dispute that she was competent in California tax law when asked to indicate whether she had expertise in California tax law.

As noted above, in order to show that it had reasonable cause for its late payment, appellant must establish that its reliance on its tax professional's advice for questions of substantive tax law was reasonable. Here, appellant has failed to do so. Namely, appellant has failed to show that its tax preparer had competency in California tax law. *(Appeal of Summit Hosting, LLC, supra*.) Appellant's tax preparer, who was based in Texas, timely filed appellant's 2018 tax return indicating that no tax franchise or income tax was due. After processing appellant's return, respondent informed appellant via letter dated January 30, 2020, that it owed the minimum franchise tax of $800, an estimated tax penalty of $30.90 and a late

payment penalty of $84.00, plus interest. Despite being provided with the relevant information to determine the liability, in a letter dated December 11, 2020, the tax preparer continued to advise appellant that the Franchise Tax was improperly imposed, indicating that appellant did not owe any tax, and thus, the late payment penalty was improperly assessed. The tax preparer did not discuss any additional research that she had conducted or provide any explanation or analysis as to why she continued to believe that the minimum franchise tax was improperly imposed by respondent.

We would expect a tax preparer with competency in California tax law to be familiar with the minimum franchise tax and to review the information provided by respondent. Moreover, appellant has not provided supporting evidence to demonstrate the steps taken by its tax preparer to ascertain whether appellant was required to pay the minimum franchise tax. Appellant has also not provided evidence to show the tax preparer's knowledge of, and experience in, California tax law.[5] Furthermore, we find that the fact that Enrolled Agents are exempted from CTEC requirements is insufficient to establish that all Enrolled Agents are knowledgeable and competent in California tax law. Therefore, based on the evidence before us, it would be unreasonable to conclude that appellant's tax preparer is competent in California tax law. As such, we find that appellant has not established that it had reasonable cause for its late payment based on advice given by its tax professional.

Appellant also contends that it provided its tax preparer with the relevant facts which is evidenced by the fact that she included certain information on the tax return at issue. For example, the date of incorporation and the date of the dissolution of the business, are relevant facts and are included on appellant's return, thus, appellant argues, that we can conclude that appellant provided this information to its tax preparer. As such, appellant argues that the fact that appellant's representative stated in an email that she could not confirm that appellant had apprised her of all relevant facts and documents is not relevant and we should conclude based on the evidence in the return that the relevant documentation was provided to the tax preparer.

It is not clear what evidence appellant provided to its tax preparer or when such evidence was provided. Further, as noted above, appellant's representative stated that she could not confirm that she was provided with the relevant facts and documentation. The burden is on

[5] At the hearing we specifically asked whether the tax preparer had any experience in preparing California tax returns and appellant answered that it did not know.

appellant to show that the tax professional's advice is based on the taxpayer's full disclosure of the relevant facts and documents. (*United States v. Boyle, supra* 469 U.S. at p. 250, *Appeal of Summit Hosting*, *supra*.) Without knowing what documentation or evidence was provided to the tax preparer to determine appellant's tax liability, we are unable to conclude that a full disclosure of the relevant facts and documents was made. Moreover, while appellant argues that the question posed to the tax preparer in the December 9, 2020 email, was incorrectly phrased, and that it would be cost prohibitive to ask the tax preparer to clarify her prior statements, this does not negate the fact that the burden is on appellant to show that it made a full disclosure of the relevant facts and documents. Here, appellant has failed to do so.

Appellant further argues that although its tax preparer was a competent professional with sufficient expertise, it is not required to show that its tax preparer was competent under *United States v. Boyle, supra*. Appellant contends that the Supreme Court in *United States v. Boyle, supra*, does not specifically state that appellant is required to show that its tax preparer was competent, but only requires that appellant have reasonably relied on the tax preparer's advice. Appellant notes that the Supreme Court states, "when an accountant or attorney advises a tax preparer on a matter of tax law, such as whether or not a liability exists, it is reasonable for the taxpayer to rely on that advice." (*United States v. Boyle, supra*, 469 U.S. at p. 251.) Respondent points out that the Supreme Court in *United States v. Boyle*, cited to *Burton Swartz Land Corp v. Commissioner* (5th Cir. 1952) 198 F.2d 558, 560) in support of the contention that "[c]ourts have frequently held that 'reasonable cause' is established when a taxpayer shows that he reasonably relied on the advice of an accountant or attorney that it was unnecessary to file a return, even when such advice turned out to have been mistaken." (*United States v. Boyle*, 469 U.S. at p. 250.) Respondent notes that Fifth Circuit *Burton Swartz* states, "It is now well settled that the advice of a competent accountant constitutes 'reasonable cause' for failure to file a tax return, and that a taxpayer who in good faith acts upon such advice, after full disclosure to the accountant, is not guilty of willful neglect." (*Burton Swartz Land Corp v. Commissioner*, *supra*, 198 F.2d at p. 560.) Appellant argues that in citing to *Burton Swartz*, the Supreme Court did not intend to impose a competency standard upon the tax preparer but rather cited to *Burton Swartz* for the proposition that, "reasonable cause" is established when a taxpayer shows that he reasonably relied on the advice of an accountant or attorney that it was unnecessary to file a

return, even when such advice turned out to have been mistaken. (*United States v. Boyle*, *supra*, 469 U.S. at p. 250.)

As noted in *United States v. Boyle*, the term reasonable cause is not defined in the code, but the relevant Treasury Regulation[6] calls on the taxpayer to demonstrate that he exercised "ordinary business care and prudence." (*United States v. Boyle*, 469 U.S. at p. 243.) The determination of whether reasonable cause exists for the late payment requires an analysis of appellant's actions leading up to the late payment, the timing of those actions, and whether they reflect ordinary business care and prudence, such as an ordinarily intelligent and prudent businessperson would have performed under similar circumstances. (*Appeal of Moren*, *supra*.) We believe an ordinarily intelligent and prudent businessperson would seek out a tax preparer that was competent in not only tax law in general, but in the tax law of the state with jurisdiction over the return at issue. Thus, we find that it would be unreasonable to conclude that a taxpayer can establish reasonable cause for abatement of the late payment penalty because it relied on the advice of their tax preparer, without also showing that the tax preparer was competent in not only tax law in general, but California tax law as well, when the liability at issue involves a California tax return.

As such, we find that appellant has not demonstrated reasonable cause for its failure to timely pay its 2018 tax liability.

Issue 3: Whether appellant has established cause to abate the underpayment of estimated tax penalty.

IRC section 6654 imposes an addition to tax, which is treated and often referred to as a penalty, where an individual fails to timely pay estimated tax. Subject to certain exceptions not relevant to the issues on appeal, R&TC section 19136 incorporates IRC section 6654. The estimated tax penalty is similar to an interest charge in that it is calculated applying the applicable interest rate to the underpayment of estimated tax. (See IRC, § 6654(a) [calculating the estimated tax penalty by reference to the interest rate imposed on underpayments]; R&TC section 19136(b) [referring to R&TC section 19521 which, with modification, conforms to the federal interest provisions in IRC section 6621].)

[6] "If the taxpayer exercised ordinary business care and prudence and was nevertheless unable to file the return within the prescribed time, then the delay is due to a reasonable cause." (Treas. Reg. section 301.6651-1(c)(1).)

There is no provision in the IRC or R&TC that allows the estimated tax penalty to be abated based solely on a finding of reasonable cause. (*Appeal of Johnson*, 2018-OTA-119P.) As a result, there is no general reasonable cause exception to imposition of the estimated tax penalty. (*Appeal of Johnson*, *supra*, *Appeal of Saltzman*, 2019-OTA-070P.) The estimated tax penalty is mandatory unless the taxpayer establishes that a statutory exception applies. (*Appeal of Johnson, supra*, *Appeal of Saltzman, supra*.) Although there is no provision allowing for abatement of the estimated tax penalty based solely on reasonable cause, IRC section 6654(e)(3)(A) provides that the taxing agency may waive the estimated tax penalty if it determines that, "by reason of casualty, disaster, or other unusual circumstances the imposition of [the estimated tax penalty] would be against equity and good conscience." Appellant has not specifically addressed the estimated tax penalty and has not provided argument or evidence that would provide a basis for waiver of the estimated tax penalty.

Issue 4: Whether appellant has established that interest should be waived or abated.

Interest must be assessed from the date a tax payment is due through the date that it is paid. (R&TC § 19101.) Imposition of interest is mandatory; it is not a penalty, but is compensation for appellant's use of money after it should have been paid to the state. (*Appeal of Moy*, 2019-OTA-057P.) Interest can only be abated in certain limited situations when authorized by law. (R&TC, § 19101(a); *Appeal of Balch*, 2018-OTA-159P.) There is no reasonable cause exception to the imposition of interest. (*Appeal of Summit Hosting, LLC supra*.) To obtain relief from interest, appellant must qualify under R&TC section 19104, 19112, or 21012; however, based on the evidence and arguments provided in this matter, none of these statutory provisions apply.[7] Thus, we find that appellant has not established any basis for waiver of abatement of interest.

[7] Pursuant to R&TC section 19104, respondent is authorized to abate or refund interest if there has been an unreasonable error or delay in the performance of a ministerial or managerial act by an employee of respondent. Here, appellant does not assert any such errors or delays occurred. Further that relief pursuant to R&TC section 21012 is not relevant here because respondent did not provide appellant with any written advice. Relief pursuant to R&TC section 19112 is not relevant here because appellant does not allege extreme financial hardship caused by significant disability or other catastrophic circumstance, which we do not have authority to review. (See *Appeal of Moy*, *supra*.)

HOLDINGS

1. Appellant is subject to the minimum franchise tax for tax year ending December 31, 2018.
2. Appellant has not established that the late payment of tax was due to reasonable cause.
3. Appellant has not established that the estimated tax penalty should be abated.
4. Appellant has not established that interest should be waived or abated.

DISPOSITION

Respondent's action in denying appellant's claim for refund is sustained.

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Natasha Ralston
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Natasha Ralston
Administrative Law Judge

We concur:

DocuSigned by:
Cheryl L. Akin
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Cheryl L. Akin
Administrative Law Judge

DocuSigned by:
Sara A Hosey
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Sara A. Hosey
Administrative Law Judge

Date Issued: 2/15/2022