

OFFICE OF TAX APPEALS
STATE OF CALIFORNIA

In the Matter of the Appeal of:

K. CHAN AND
I. CHAN

) OTA Case No. 21098592
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OPINION

Representing the Parties:

For Appellants: K. Chan and I. Chan

For Respondent: Christopher T. Tuttle, Tax Counsel

A. LONG, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19324, K. Chan and I. Chan (appellants) appeal an action by respondent Franchise Tax Board (FTB) denying appellants’ claim for refund of \$1,882 for the 2019 tax year.¹

Appellants elected to have this appeal determined pursuant to the procedures of the Small Case Program. Those procedures require the assignment of a single administrative law judge. (Cal. Code Regs., tit. 18, § 30209.1.) Appellants waived the right to an oral hearing; therefore, the matter is being decided based on the written record.

ISSUE

Whether appellants have established reasonable cause to abate the dishonored payment penalty under R&TC section 19134.

FACTUAL FINDINGS

1. On July 15, 2020, appellants remitted an extension payment of \$94,000 through FTB's Electronic Funds Transfer (EFT) Web Payment system. FTB applied this payment of \$94,000 toward the 2019 tax year.

¹ The claim for refund requests abatement of a dishonored payment penalty of \$1,881.80 imposed for the 2019 tax year.

2. On July 16, 2020, another attempt to remit \$94,000 to FTB was made, but the payment was dishonored by appellants' bank and, therefore, not remitted to FTB.
3. In a State Income Tax Balance Due Notice, FTB informed appellants that it had imposed a dishonored payment penalty of \$1,881.80.
4. On August 19, 2020, appellants remitted a payment of \$1,882, which satisfied the dishonored payment penalty.
5. On May 15, 2021, appellants filed a claim for refund of the dishonored payment penalty in which they argued that the penalty be abated for reasonable cause. Appellants asserted that when they paid estimated tax of \$94,000 with their 2019 filing extension form on July 15, 2020, their bank "account was incorrectly debited twice for that amount on July 20, 2020." Appellants asserted that as a result of the second payment of \$94,000, their account became overdrawn, which caused FTB to impose the penalty. Appellants asserted that they had sufficient funds in their account for the intended one time \$94,000 tax payment. Instead, they assert that they were unexpectedly charged two times in that amount. Appellants attached a letter dated May 11, 2021, from the manager of a branch of Citibank N.A. in Berkeley, California, stating that the payment of \$94,000 to FTB on July 20, 2020, was only meant to be paid once but was incorrectly paid twice.
6. FTB denied appellants' claim for refund. Appellants subsequently filed this timely appeal.

DISCUSSION

When taxpayers provide a check to FTB that is subsequently dishonored, a penalty is assessed against the taxpayers unless they can show that the check was tendered "in good faith and with reasonable cause to believe that it would be duly paid." (Internal Revenue Code (IRC), § 6657.)² This penalty is often referred to as the dishonored payment penalty.

As with other penalties containing a "reasonable cause" exception, the taxpayers bear the burden of proving the existence of reasonable cause. (See *Appeal of Xie*, 2018-OTA-076P.) The taxpayers must provide credible and competent evidence to support the claim of reasonable cause; otherwise, the penalty cannot be abated. (*Ibid.*) The taxpayers bear the burden of proving

² The federal penalty is incorporated into California law under R&TC section 19134. R&TC section 19134(b) adds that IRC section 6657 also applies to payments made by credit card or EFT.

that an ordinarily intelligent and prudent businessperson would have acted similarly under the circumstances. (*Appeal of Friedman*, 2018-OTA-077P.)

Here, it is undisputed that appellants' second payment of \$94,000 to FTB was dishonored because appellants had insufficient funds in their bank account to remit this amount. As such, the penalty was properly imposed.

Appellants assert that they did not intend to make the second EFT payment of \$94,000, but that this second payment resulted from the error of appellants' CPA who prepared a duplicate extension request to FTB for the 2019 tax year without appellants' knowledge.

The standard for reasonable cause for a dishonored payment penalty is predicated on an assumption the taxpayers have an outstanding liability with FTB, and the penalty can be abated if it is shown that taxpayers reasonably believed that the amount tendered would be paid. However, it does not contemplate a situation where no payment was ever due to be paid to FTB in the first place and, consequently, the statute does not mitigate or excuse the taxpayers' error for submitting duplicative payments.

The IRS, in contrast, allows the dishonored payment penalty to be abated under its discretionary powers. The IRS's Internal Revenue Manual states that in certain situations, such as "posting of duplicate transactions and only one was honored," the IRS may abate the dishonored payment penalty under IRC section 6404(a)(3), which states, "The [IRS] is authorized to abate the unpaid portion of the assessment of any tax or any liability in respect thereof, which is erroneously or illegally assessed." (See Internal Revenue Manual § 20.1.10.7.3(1)(a).)³

However, even if FTB has similar discretionary authority to abate an assessment that may have been "erroneously or illegally assessed," OTA cannot compel FTB to abate a penalty, or review FTB's failure to abate a penalty, without explicit statutory authority. (See *Appeal of Moy*, 2019-OTA-057P [holding that OTA cannot review a purely discretionary act without a meaningful standard against which to judge the agency's exercise of that discretion].) OTA can only analyze whether the dishonored payment penalty can be abated under the limited circumstance described in IRC section 6657. As such, regardless if an honest mistake occurred when appellants' CPA prepared a duplicate extension request, the penalty cannot be abated

³ It is noted that the IRS has also imposed a dishonored payment penalty for appellants' 2019 tax year, which has not been abated according to the IRS Account Transcript.

because appellants did not tender the second payment in good faith and with reasonable cause to believe that it would be duly paid pursuant to IRC section 6657.

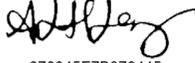
Appellants also contend that imposing “a full penalty” is unjust here because it does not consider appellants’ special circumstances where they had no bad motive. Appellants seem to suggest that a reduced penalty would be more appropriate. However, as explained above, the only basis to abate the penalty is upon a finding of reasonable cause under IRC section 6657. Because appellants cannot meet this exception, the penalty cannot be abated.

HOLDING

Appellants have not established reasonable cause to abate the dishonored payment penalty under R&TC section 19134.

DISPOSITION

FTB’s action is sustained.

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Andrea L.H. Long
Administrative Law Judge

Date Issued: 4/21/2022