

**OFFICE OF TAX APPEALS  
STATE OF CALIFORNIA**

In the Matter of the Appeal of: ) OTA Case No. 21078260  
A. GHANIEZADEH AND )  
M. GHANIEZADEH )  
\_\_\_\_\_ )

**OPINION**

Representing the Parties:

For Appellants: A. Ghaniezadeh and M. Ghaniezadeh

For Respondent: Anne Mazur, Specialist

For Office of Tax Appeals: Nguyen Dang, Tax Counsel III

K. GAST, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19045, A. Ghaniezadeh and M. Ghaniezadeh (appellants) appeal an action by respondent Franchise Tax Board (FTB) proposing an accuracy-related penalty of \$9,752.40, plus applicable interest, for the 2015 tax year.<sup>1</sup>

Appellants waived their right to an oral hearing; therefore, Office of Tax Appeals (OTA) decides the matter based on the written record.

**ISSUE**

Whether the accuracy-related penalty and interest should be abated.

**FACTUAL FINDINGS**

1. FTB audited appellants’ joint 2015 California resident income tax return and increased their taxable income by \$556,684 based on two adjustments: (1) \$273,637 related to gain from an Internal Revenue Code (IRC) section 1031 exchange they recognized and

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<sup>1</sup> In their appeal letter, appellants indicate they “would like to appeal [FTB’s] proposed tax assessment of \$70,451.86,” which includes additional tax of \$48,762. However, appellants raise no arguments disputing FTB’s proposed assessment of additional tax. Therefore, OTA does not discuss it further and instead focuses on the penalty and interest appellants specifically dispute.

- reported on their federal tax return but subtracted from their California tax return; and (2) \$283,047 that further increased their gain related to the IRC section 1031 exchange because they failed to substantiate alleged capital expenditures and thus overstated their adjusted basis (and understated their taxable gain) in the relinquished property.<sup>2</sup>
2. Based on this determination, FTB issued a Notice of Proposed Assessment (NPA) that increased appellants' tax liability from \$0, as reported on their original California return, to \$50,729, as adjusted by FTB. The NPA further imposed an accuracy-related penalty, plus applicable interest.
  3. Appellants protested the NPA, which FTB subsequently sustained by issuing a Notice of Action, except FTB reduced the additional tax to \$48,762 and the accuracy-related penalty to \$9,752.40.<sup>3</sup> Appellants filed a timely appeal seeking only penalty and interest abatement.

### DISCUSSION

Appellants provide several reasons why the accuracy-related penalty and interest should be abated. They assert their inability to substantiate various capital expenditures, which would have reduced the amount of understated taxable gain, was due to the loss of various business records and receipts in a fire. They argue this is the first time they have underpaid their taxes and this error was done in good faith and not intentional. They further contend they are unable to pay the liability due to financial difficulties arising from the COVID-19 pandemic.

California conforms to IRC section 6662, which imposes an accuracy-related penalty of 20 percent of the applicable underpayment. (R&TC, § 19164(a)(1)(A)-(B).) As relevant here, the penalty applies to the portion of the underpayment attributable to any “substantial understatement of income tax.” (IRC, § 6662(b)(2).) For individuals, a substantial understatement of income tax is defined as an understatement that exceeds the greater of 10 percent of the tax required to be shown on the return for the taxable year, or \$5,000. (IRC, § 6662(d)(1)(A)(i)-(ii).) An “understatement” is defined as the excess of the amount of tax

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<sup>2</sup> It is unclear, based on the limited record, why appellants were required to recognize gain related to the IRC section 1031 exchange.

<sup>3</sup> This reduction occurred because during appellants' protest, FTB reduced the audited, additional gain of \$283,047 to \$263,947.

required to be shown on the return for the tax year over the amount of the tax imposed which is shown on the return, reduced by any rebate. (IRC, § 6662(d)(2)(A)(i)-(ii).)

Here, there was an understatement of tax of \$48,762, which is \$48,762 of tax required to be shown on appellants' California return less \$0 of tax they reported on that return. This \$48,762 understatement exceeds \$5,000, which is the greater of 10 percent of the tax required to be shown on the return of \$4,876.20 (i.e., 10 percent of \$48,762) or \$5,000. Therefore, OTA finds appellants substantially understated their tax.

One relevant exception to the accuracy-related penalty is that it shall not apply to any portion of the underpayment if it is shown there was reasonable cause for such portion and the taxpayer acted in good faith with respect to such portion. (IRC, § 6664(c)(1); R&TC, § 19164(d)(1).) A determination of whether a taxpayer acted with reasonable cause and in good faith is made on a case-by-case basis, taking into account all pertinent facts and circumstances. (Treas. Reg. § 1.6664-4(b)(1).) Generally, the most important factor is the extent of the taxpayer's effort to assess the taxpayer's proper tax liability. (*Ibid.*) Reasonable cause may include an honest misunderstanding of fact or law that is reasonable in light of all of the facts and circumstances, including the taxpayer's experience, knowledge, and education. (*Ibid.*)

Appellants' underpayment is attributable to both an erroneous subtraction from their California taxable income of gain related to a like-kind exchange and an understatement of additional taxable gain related to that exchange. Appellants offer no explanation why they excluded such gain from their California taxable income, or on what basis they believed such gain was not taxable under California law. They also have not explained how, in the absence of any records, they computed their adjusted basis in the relinquished property giving rise to the taxable gain. Their only contention—that substantiating records were lost in a fire—is unavailing. (See *Xuncax v. Commissioner*, T.C. Memo. 2001-226 [absence of records due to loss or destruction cannot, standing alone, establish a taxpayer's reporting position was based on reasonable cause and good faith for purposes of abating the accuracy-related penalty].) Accordingly, OTA is unable to determine whether appellants acted with reasonable cause and in good faith with respect to any portion of the underpayment.

With respect to interest, its imposition is mandatory and accrues regardless of the reason for the deficiency. (R&TC, § 19101(a); *Appeal of Balch*, 2018-OTA-159P.) There is no reasonable cause exception to its imposition. (*Appeal of Moy*, 2019-OTA-057P.) Therefore, to

obtain interest relief, appellants must qualify under one of the waiver provisions: R&TC section 19104 (pertaining to unreasonable error or delay by FTB in the performance of a ministerial or managerial act); or 21012 (pertaining to reasonable reliance on written advice of FTB).<sup>4</sup> (*Ibid.*) Appellants do not allege, and the record does not reflect, these waiver provisions are applicable here. Thus, OTA finds there is no basis for abating interest.

Lastly, appellants assert this is the first time they have had a California tax issue. However, California does not allow for a “first-time” abatement of penalties or interest (*Appeal of Porreca*, 2018-OTA-095P), and OTA is unable to relieve appellants of these items based on financial hardship or inability to pay (*Appeal of Robinson*, 2018-OTA-059P).

For the reasons expressed above, OTA finds appellants have not established any basis for abating the accuracy-related penalty or interest.

HOLDING

The accuracy-related penalty and interest should not be abated.

DISPOSITION

FTB’s action is sustained.

DocuSigned by:  
*Kenneth Gast*  
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Kenneth Gast  
Administrative Law Judge

We concur:

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

DocuSigned by:  
*Eddy Y.H. Lam*  
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Eddy Y.H. Lam  
Administrative Law Judge

Date Issued: 5/18/2022

<sup>4</sup> Although appellants do not allege R&TC section 19112 is applicable here, that provision allows FTB to waive interest related to extreme financial hardship caused by significant disability or other catastrophic circumstance. However, OTA does not have authority to review FTB’s denial of a waiver of interest under that provision. (*Appeal of Moy, supra.*)