OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

In the Matter of the Appeal of: **R. SULLIVAN**	OTA Case No. 21047695

OPINION

Representing the Parties:

For Appellant: Elizabeth Gonsalves, Esq.

For Respondent: Eric R. Brown, Tax Counsel III

M. GEARY, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19324, R. Sullivan (appellant) appeals an action by the Franchise Tax Board (respondent) denying appellant's claim for refund of a $12,064 underpayment of estimated tax penalty (the penalty) for the 2019 tax year.

The matter is being decided on the basis of the written record because appellant waived the right to an oral hearing.

ISSUE

Should the estimated tax penalty be abated?

FACTUAL FINDINGS

1. By agreement dated November 6, 2019 (the "Agreement"), appellant sold his company.
2. Appellant used the services of accounting and legal professionals to complete the sale of the business and relied on them to timely and accurately calculate and pay his 2019 estimated taxes.
3. Appellant and the buyer were involved in managing the day-to-day operations of the business during the transition of ownership and in the business planning after the close of escrow.

4. According to appellant, escrow closed late in the 2019 year.[1] Appellant provided only eight pages of the 46-page Agreement. He has not provided the parts of the Agreement that discuss the close of escrow.
5. Appellant's 2019 California taxable income was more than 20 times higher than he had earned in any prior year.
6. Around the time escrow closed on the sale of his business, appellant entered into an agreement to provide mechanical engineering and consulting services in Malaysia. Appellant travelled to Canada several times between September 18, 2019, and November 22, 2019, in connection with and preparation for the planned work in Malaysia.
7. Appellant flew from the U.S. to Malaysia on December 4, 2019.[2] Appellant returned to the U.S. on January 8, 2020, and then returned to Malaysia again on January 18, 2020, where he remained until at least July 27, 2021.[3]
8. Prior to filing the 2019 return, appellant's employer remitted amounts withheld from appellant's wages earned. In addition, appellant made a 2019 estimated tax payment on June 11, 2019, and a second estimated tax payment on January 10, 2020. These estimated tax and withholding payments totaled just over 65 percent of the estimated tax payments that were due by January 15, 2020.
9. Appellant timely filed his California Resident Income Tax Return on October 15, 2020. The return self-reports the penalty of $12,064 and includes a completed Form 5805, which states that appellant was not requesting a waiver of the penalty. The return also reports an overpayment of tax totaling $100,357 and requests that $88,293 of that amount be applied to appellant's 2020 estimated tax, leaving $12,064 "available" for 2019 liabilities.
10. Appellant filed a claim for refund of the penalty on December 15, 2020.

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[1] Appellant has not provided the actual closing date.

[2] Appellant states that he left the U.S. on December 5, 2019, but the itinerary states he left on December 4, 2019.

[3] Appellant states in his "Declaration," that he traveled from Malaysia to the U.S. on December 20, 2019, but contradicts that statement in a footnote where he states that his December flight to return to the U.S. was changed to January 8, 2020. Appellant provided copies of itineraries consistent with some of this travel.

11. On January 21, 2021, respondent sent appellant a Notice of Tax Return Change – No Balance to inform appellant that there was no balance overpaid for 2019 after payment of the taxes and the penalty, and therefore there was nothing to apply to 2020 estimated payments.[4]
12. By letter dated January 28, 2021, respondent denied appellant's claim for refund. This timely appeal followed.

DISCUSSION

Internal Revenue Code (IRC) section 6654 imposes an addition to tax where an individual fails to timely pay estimated tax. California generally conforms to the federal law in this respect. (R&TC, § 19136, et seq.) While the estimated tax penalty is treated and often referred to as a penalty, section 6654 refers to it as an "addition to tax," which is calculated by applying the applicable interest rate to the underpayment of estimated tax.[5] Subject to certain exceptions not relevant here, respondent must impose a penalty on a taxpayer who fails to make adequate estimated tax payments. (*Ibid*.) This penalty is typically imposed when an individual filer still owes $250 or more in taxes after credit for all installment payments, including amounts withheld through payroll deductions and amounts paid in periodic installments. (R&TC, § 19136(c)(2).)

While IRC section 6654(c) prescribes four payments (April 15, June 15, and September 15 of the tax year and January 15 immediately following the tax year), California requires three estimated tax payments: 30 percent (of the required total payment) on or before April 15 of the tax year; 40 percent on or before June 15 of the tax year; and the final 30 percent on or before January 15 immediately following the tax year. (R&TC, § 19136.1.)[6]

[4] Respondent indicates it has nevertheless placed the $88,293 in suspense pending conclusion of this appeal.

[5] See IRC, § 6654(a) [calculating the estimated tax penalty by reference to the interest rate imposed on underpayments] and Section 19136(b) [referring to Section 19521 which, with modification, conforms to the federal interest provisions in IRC section 6621].

[6] R&TC section 19136.1 also refers to a payment on September 15 of the tax year, but it indicates the amount due as "zero."

R&TC section 19136.3 provides that in the case of an individual reporting adjusted gross income (AGI) greater than $1 million, the required annual payment is 90 percent of the tax shown on the return for the taxable year.[7]

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, and there is no general reasonable cause exception to imposition of the estimated tax penalty. (*Appeal of Johnson*, 2018-OTA-119P.) However, 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."[8] In this context, OTA interprets the terms "casualty" and "disaster" to refer to unexpected events, which cause a loss or hardship that, depending on the circumstance, may make it inequitable to apply the penalty; and it interprets the less specific words, "unusual circumstances," to refer to circumstances or events similar to the more specific terms that precede them. (*Appeal of Johnson*, 2018-OTA-119P.) Circumstances that have been found not sufficient to warrant abatement include: stock market volatility, including huge losses like those resulting from the 2000 dot.com crash (*Farhoumand v. Commissioner*, T.C. Memo. 2012-131); good faith belief that income would not be subject to California income tax (*Appeal of Saltzman*, 2019-OTA-070P); and a "once in a lifetime" substantial capital gain from the sale of property (*Appeal of Johnson*, *supra*).

It does not appear that appellant argues that a casualty prevented the timely payment of the estimated tax, though his argument does combine elements of the other two statutory reasons: disaster and other unusual circumstances. Appellant argues that the penalty should be abated because a combination of the following circumstances combined to prevent him from timely paying the required estimated taxes:

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[7] As relevant, California does not fully conform to the federal safe harbor in IRC section 6654(d)(1)(B)(ii), for taxpayers making a required annual payment of 110 percent of the tax shown on the return for the prior year. R&TC section 19136.3 provides that for tax years beginning on or after January 1, 2009, the federal safe harbor in IRC section 6654(d)(1)(B)(ii) does not apply to individuals reporting California AGI in excess of $1 million. The California AGI threshold is $500,000 in the case of a married individual filing a separate return. (R&TC § 19136.3(a).) Appellants reported California AGI of $58,531,222; thus, the safe harbor does not apply to them.

[8] IRC section 6654(e)(3)(B) provides another potential avenue for waiver of the penalty where the taxing agency determines that (i) during the applicable tax year or the preceding year, the taxpayer either retired after having attained age 62, or became disabled, and (ii) the underpayment was due to "reasonable cause" and not due to willful neglect. However, there is no evidence or argument that this provision should apply.

- The sale of appellant's business less than two months before the end of the 2019 tax year, resulting in 2019 income many times higher than in any prior year
- A complicated calculation of appellant's income and gain for 2019
- The unavailability of 2019 tax software until after January 15, 2019
- The unavailability of income data from the buyer of the business
- Appellant's absence from the U.S. for work in Malaysia
- Unreliable modes of communication between appellant's work location in Malaysia and persons working to calculate the estimated taxes
- Travel restrictions arising from, and appellant's own health concerns regarding, the COVID-19 pandemic
- The inaccessibility of appellant's business records in California, which former President Trump declared a federally recognized disaster area in March 2020, and
- The applicability to appellant, for the first time, of the Mental Health Services (MHS) Tax.

Before we examine these circumstances and events in detail, we note that generally, respondent's imposition of a penalty is presumed to be correct until the taxpayer proves otherwise. (*Appeal of Xie*, 2018-OTA-076P.) Likewise, a taxpayer who claims a refund has the burden of proving his or her entitlement to the refund. (*Appeal of Estate of Gillespie*, 2018-OTA-052P.)[9] Unsupported assertions are not sufficient to satisfy the burden of proof. (*Appeal of Davis and Hunter-Davis*, 2020-OTA-182P.) To prevail, appellant must prove the necessary facts by a preponderance of the evidence, meaning the evidence must prove that the purported facts are more likely than not correct. (Cal. Code Regs., tit. 18, § 30219(c); *Concrete Pipe and Products of California, Inc. v. Construction Laborers Pension Trust for Southern California* (1993) 508 U.S. 602, 622.)

Here, the evidence does not establish some of the facts relied upon by appellant, and such facts are, in any event, not relevant to our analysis. Appellant concedes he did not timely pay the correct amount of estimated tax and does not argue that respondent incorrectly calculated the

[9] Similarly, the Office of Tax Appeals' Rules for Tax Appeals state that except as specifically provided by law, the burden of proof as to all issues of fact rests with appellant. (Cal. Code Regs., tit. 18, § 30219(a).)

addition to tax. Appellant contends that the calculation of his income and gain for 2019 was complicated, but the evidence does not support that contention. (See *Appeal of Moren*, 2019-OTA-176P.) The Agreement contains the purchase price for the business and the other primary elements of appellant's 2019 income (wages, interest, ordinary dividends) that should have been known to appellant by the end of the 2019 tax year. The same is true of appellant's bare assertion that he needed income information from the buyer, or that estimated tax could not be calculated without 2019 tax preparation software. Appellant has failed to provide persuasive arguments or evidence that any of these alleged facts is true. More importantly, though, these kinds of extenuating circumstances, while potentially relevant to a reasonable cause analysis, are not relevant to the question before us. (*Appeal of Mazdyasni*, 2018-OTA-049P.) We find that none of these alleged unusual circumstances are established by the evidence and that none of them provide a basis for relief under IRC section 6654(e)(3)(A).

We also are not persuaded by the evidence that appellant's presence in the U.S. or access to appellant's records was required to calculate the estimated tax payment. On the contrary, the converse is probably true, as evidenced by the fact that the correct extension payment[10] was made the day before the due date while appellant was still in Malaysia and his records were still in California. Furthermore, appellant was present in California before December 4, 2019, and again for about a week before the January 15, 2020 estimated tax payment was due. The evidence does not show why appellant could not work with his advisors to correctly calculate that payment before he left for Malaysia on January 18, 2020.

Appellant's argument that the COVID-19 pandemic prevented appellant from timely paying the estimated tax is not supported by the evidence. Appellant was in the U.S, before December 4, 2019, for a week before the January 15, 2020 payment was due, and for a few days thereafter. There is no evidence that travel was restricted during that time (or for at least weeks thereafter) due to COVID-19. We see no relevant connection between COVID-19 travel restrictions, or our former President's March 2020 disaster declaration involving COVID-19, and California, and appellant's failure to timely pay the estimated tax by January 15, 2020. Consequently, we find that appellant's failure to timely pay the estimated tax was not caused by the COVID-19 pandemic or by any related travel restrictions or declaration.

[10] The extension payment equaled the remainder of the tax due plus the penalty.

Appellant correctly points out that, while the penalty was required for any estimated tax underpayment after January 15, 2020, the amount of the penalty increased with the time that passed between the due date and the July 15, 2020 tax payment due date.[11] It is on that basis that he argues that the later travel restrictions – and his own reluctance to travel from what he considered his safe place in Malaysia – should be considered unusual circumstances that prevented him from paying the estimated tax before July 14, 2020, the day before the final tax payment was due. However, this argument is unpersuasive for the same reason that appellant's other arguments fail: a failure of proof. Appellant has failed to prove how the January 2020 payment was miscalculated or why it was not correctly calculated and paid by the due date, and he has failed to prove why he could not have made the payment from his location in Malaysia, just as he did on July 14, 2020.

Regarding appellant's argument that his failure to timely pay the estimated tax was due in part to the first-time assessment of the MHS Tax, we note only that this tax had been in effect for many years prior to the year at issue,[12] and there could have been no question in the minds of appellant's accounting and legal advisors that the tax would apply to appellant. It should simply have been part of the calculation that should have been done before the January 2020 payment.

For the reasons stated above, we find that appellant has not carried his burden to prove that the penalty should be abated.

[11] Individual income taxes are generally due by April 15 of the year immediately following the tax year. However, respondent issued a March 18, 2020 News Release that confirmed an extension of the 2019 tax filing and payment deadlines for all Californians to July 15, 2020.

[12] See R&TC section 17043.

HOLDING

The estimated tax penalty should not be abated.

DISPOSITION

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

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Michael F. Geary
Administrative Law Judge

We concur:

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Keith T. Long
Administrative Law Judge

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Richard Tay
Administrative Law Judge

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