

OFFICE OF TAX APPEALS
STATE OF CALIFORNIA

In the Matter of the Appeal of:

R. AUGUSTA AND
S. AUGUSTA HUYNH) OTA Case No. 22039886
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)**OPINION**

Representing the Parties:

For Appellants:

R. Augusta
S. Augusta Huynh

For Respondent:

Alisa L. Pinarbasi, Tax Counsel

K. LONG, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19045, R. Augusta and S. Huynh (appellants) appeal an action by respondent Franchise Tax Board (FTB) denying appellants' claim for refund of \$19,022.52 for the 2019 tax year.¹

Appellants waived the right to an oral hearing; therefore, the matter is being decided based on the written record.

ISSUES

1. Whether appellants have established reasonable cause for failing to make a timely payment of tax for the 2019 tax year.
2. Whether appellants have established a basis to abate the underpayment of estimated tax penalty (estimated tax penalty).

¹ Appellants' claim for refund seeks a refund of \$9,367.92. However, the late payment penalty that FTB imposed in its September 14 2020 Notice of Tax Return Change – Revised Balance was \$10,821.12. Further, the late payment penalty consists of two parts including a 5 percent penalty of the "total unpaid tax" and a .5 percent monthly penalty of "the remaining tax" for each additional month or fraction thereof not to exceed 40 months during which "the remaining tax" is greater than zero. (R&TC, 19132(a)(2).) As appellants made installment payments on their liability, the penalty increased. To that end, FTB's denial is in the amount of \$18,385.52 (the total amount of the late payment penalty). However, on appeal, it appears that both the late payment penalty and the estimated tax penalty are in dispute. As such, OTA finds that the amount in dispute is \$19,022.52.

FACTUAL FINDINGS

1. Appellants filed a timely joint 2019 income tax return, within the extension period, reporting a tax of \$213,884. After applying withholding credits and payments, appellants reported a balance due of \$180,352.
2. On September 14, 2020, FTB issued a Notice of Tax Return Change – Revised Balance, imposing a late payment penalty of \$10,821.12, an estimated tax penalty of \$637.00, and interest.
3. Appellants made tax payments satisfying the liability during the period September 22, 2020, through July 28, 2021. In total, appellants paid \$18,385.52 for the late payment penalty and \$637.00 for the estimated tax penalty.
4. Appellants filed a timely claim for refund dated August 17, 2021, requesting abatement of the penalties.
5. FTB denied appellants’ claim for refund. This timely appeal followed.

DISCUSSION

Issue 1: Whether appellants have established reasonable cause for failing to make a timely payment of tax for the 2019 tax year.

R&TC section 19001 generally provides that the personal income tax imposed “shall be paid at the time and place fixed for filing the return (determined without regard to any extension of time for filing the return).” R&TC section 19132 provides that a late payment penalty must be imposed when taxpayers fail to pay the amount shown as due on the return on or before the due date of the return.

The late payment penalty will be abated if the taxpayers show that the failure to make a timely payment of tax was due to reasonable cause and was not due to willful neglect. (R&TC, § 19132(a).) Taxpayers bear the burden to show that reasonable cause exists to abate the late payment penalty. (*Appeal of Friedman*, 2018-OTA-077P.) To establish reasonable cause for the late payment of tax, taxpayers must show that the failure to make a timely payment of the proper amount of tax occurred despite the exercise of ordinary business care and prudence. (*Appeal of Friedman, supra.*) Appellants bear the burden of proving that an ordinarily intelligent and prudent businessperson would have acted similarly under the circumstances.

Financial hardship may constitute reasonable cause to excuse the late payment of tax. (*Appeal of Rougeau*, 2021-OTA-335P.) Reasonable cause based on financial hardship is explained in federal Treasury Regulation section 301.6651-1(c)(1), which provides that the taxpayer must show the exercise of ordinary business care and prudence and that the taxpayer was either unable to pay the tax or would suffer an undue hardship by paying by the due date.² Treasury Regulation section 301.6651-1(c)(1) further provides that all the facts and circumstances will be considered, including the amount and nature of the taxpayers' expenditures in light of the income (or other amounts) the taxpayer could, at the time of such expenditures, reasonably expect to receive prior to the date prescribed for the payment of the tax. Thus, taxpayers can prove ordinary business care and prudence by showing reasonable efforts to conserve sufficient assets in marketable form to satisfy the tax liability. (*Ibid.*) However, taxpayers who invest funds in speculative or illiquid assets have not exercised ordinary business care and prudence in providing for the payment of their tax liability unless, at the time of the investment, the remainder of the taxpayers' assets and estimated income will be sufficient to pay or it can be reasonably foreseen that the speculative or illiquid investment made by the taxpayer can be utilized (by sale or as security for a loan) to realize sufficient funds to satisfy the tax liability. (Treas. Reg. 301.6651(c)(1).)

Here, the late payment penalty was properly imposed because appellants failed to pay their tax liability by the due date of June 15, 2020.³ Nevertheless, appellants assert that there is reasonable cause for their late payment. Specifically, appellants assert that their tax liability stems from stock options granted to them in 2008. Appellants state that they exercised the stock options in 2019, before they expired, which triggered a tax event even though they received no actual income from the transaction. Appellants concede that they were aware that exercising the stock options would result in a large tax liability. However, appellants argue that the resulting tax liability was greater than both of their incomes combined and that there was no market for

² Although there are no FTB regulations interpreting R&TC section 19132, that section is patterned after Internal Revenue Code section 6651. Therefore, the interpretation and effect given the federal provision by the federal courts and administrative bodies are relevant in determining the proper construction of the California statute. (*Andrews v. Franchise Tax Bd.* (1969) 275 Cal.App.2d 653, 658; *Rihn v. Franchise Tax Bd.* (1955) 131 Cal.App.2d 356, 360.)

³ For the 2019 tax year, FTB extended the due date for payment of individual tax liabilities from April 15, 2020, to June 15, 2020. (<https://www.ftb.ca.gov/about-ftb/newsroom/news-releases/2020-2-more-time-to-file-pay-for-california-taxpayers-affected-by-the-covid-19-pandemic.html>.)

the stock. Appellants also argue that they were “caught in an unintended rare situation that would make it impossible for almost anyone to pay their full tax bill on time.”

Appellants assert that they exercised ordinary business care and prudence with respect to their stock options. For example, appellants assert that by waiting to exercise their stock options, they “took the least speculative action possible without forfeiting a significant asset.” Appellants also argue that many considerations were incorporated into the timing of their action. However, whether appellants acted as reasonably prudent businesspeople with respect to their exercising of stock options is not in question here. Instead, the question is whether appellants’ failure to make a timely payment of the proper amount of tax occurred despite the exercise of ordinary business care and prudence. (*Appeal of Friedman, supra.*)

As discussed above, appellants exercised stock options knowing that it would trigger a large tax liability even though they received no actual income. There is no evidence that the remainder of appellants assets and estimated income were sufficient to pay the tax liability as required by Treasury Regulation 301.6651(c)(1). There is also no evidence that appellants could sell the stock shares or obtain a loan with them. (Treas. Reg. 301.6651(c)(1).) Moreover, appellants concede that there was no market for the stock shares, and a sale was not possible. Instead, appellants assert that their combined incomes were insufficient to make a complete payment of the tax liability. As such, appellants’ failure to timely pay was not due to reasonable cause.

Issue 2: Whether appellants have established a basis to abate the estimated tax penalty.


Except as otherwise provided, R&TC section 19136 conforms to Internal Revenue Code (IRC) section 6654 and imposes a penalty for the underpayment of estimated tax where a taxpayer’s installment payments are less than the amounts due at the end of the installment periods. Here, appellants make the same reasonable cause arguments as they do above. However, 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 Saltzman, 2019-OTA-070P.*) OTA, therefore, finds that appellants have not established a basis to abate the estimated tax penalty.

HOLDINGS


1. Appellants have not established reasonable cause for their failure to make a timely payment of tax for the 2019 tax year.
2. Appellants have not established a basis to abate the estimated tax penalty.


DISPOSITION

FTB’s denial of the claim for refund is sustained.

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 Keith T. Long
 Administrative Law Judge

We concur:

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 Asaf Kletter
 Administrative Law Judge

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 Josh Aldrich
 Administrative Law Judge

Date Issued: 12/27/2022