

OFFICE OF TAX APPEALS
STATE OF CALIFORNIA

In the Matter of the Appeal of:
FMI CORPORATION

) OTA Case No. 220510490
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)

OPINION

Representing the Parties:

For Appellant: Rick Najjar, Representative

For Respondent: Christopher M. Cook, Attorney

S. HOSEY, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19324, FMI Corporation (appellant) appeals actions by respondent Franchise Tax Board (FTB) denying appellant’s claims for refund of \$11,943.50 for the 2014 tax year; \$8,963.50 for the 2015 tax year; \$9,279.75 for the 2016 tax year; \$9,727.00 for the 2017 tax year; and \$11,620.25 for the 2018 tax year.

Office of Tax Appeals (OTA) Administrative Law Judges Sara A. Hosey, Kenneth Gast, and Lauren Katagihara held an electronic oral hearing for this matter on July 19, 2023. At the conclusion of the hearing, the record was closed and this matter was submitted for an opinion.

ISSUE

Whether appellant has established reasonable cause to abate the late filing penalties pursuant to R&TC section 19131 and the per-shareholder late filing penalties pursuant to R&TC section 19172.5, imposed for the 2014 through 2018 tax years.

FACTUAL FINDINGS

1. For the tax years at issue, appellant was taxed as an S Corporation and incorporated in North Carolina. It registered with the California Secretary of State (SOS), expecting to open an office in California.¹
2. Appellant untimely filed its 2014 through 2018 California tax returns on June 26, 2020. Appellant made tax payments for the tax years at issue by June 26, 2020.
3. FTB imposed late filing penalties and per-shareholder late filing penalties for each tax year at issue. Appellant paid in full all penalties and applicable interest.
4. Appellant filed claims for refund with FTB seeking abatement of the penalties, which FTB denied.
5. This timely appeal followed.

DISCUSSION

California imposes a penalty for failure to file a return by its due date, unless the failure was due to reasonable cause and not due to willful neglect. (R&TC, § 19131.) When FTB imposes a late filing penalty, it is presumed to have been correctly imposed, and the burden of proof is on the taxpayer to show that reasonable cause exists to abate the penalty. (*Appeal of Xie*, 2018-OTA-076P.) To establish reasonable cause, a taxpayer must show that the failure to file timely returns occurred despite the exercise of ordinary business care and prudence, or that cause existed as would prompt an ordinarily intelligent and prudent businessperson to have so acted under similar circumstances. (*Appeal of GEF Operating, Inc.*, 2020-OTA-057P (*GEF Operating*)). Ignorance of a filing requirement or a misunderstanding of the law generally does not excuse a late filing. (*Ibid.*)

Appellant requests abatement of the late filing penalties due to reasonable cause. Specifically, appellant asserts it did not timely file its 2014 through 2018 California S Corporation tax returns because it is an out-of-state company that was unaware it was subject to California tax, and therefore had a filing requirement during those years. Appellant contends that it stopped filing tax returns after the 2005 tax year because it abandoned its plan to open an

¹ Appellant initially registered with the SOS on January 23, 1995. Appellant was revived in 2005 after being suspended in 2000. Appellant was again suspended in 2007 after failing to file its annual statement of information. There is no record of appellant's attempt to withdraw its registration with the SOS, such as a certificate of cancellation of registration.

office in California due to various business reasons. Appellant asserts that during this time it made the determination that it no longer had nexus in California due to its lack of physical presence in the state. Appellant alleges that although it registered to do business in California with the SOS, it attempted to prepare and file documents to withdraw from the SOS, but apparently was unsuccessful in doing so. Appellant argues it was unaware of the law change in 2011 that required California tax returns to be filed even when the taxpayer did not have a physical presence in this state.² Appellant maintains that once it became aware it had economic nexus in California and therefore a filing requirement for the tax years at issue, it paid all taxes due after it unsuccessfully applied for the voluntary disclosure program with FTB. FTB did not allow appellant into the program because it was still registered with the SOS and therefore could not get the penalties at issue here abated.

A review of the record does not show any facts or circumstances that would warrant a finding of reasonable cause. Although appellant may have had a sincere belief that it was not required to file California tax returns, ignorance of a filing requirement or a misunderstanding of the law generally does not excuse a late filing. (*GEF Operating, supra.*) To establish reasonable cause, a taxpayer must show that the failure to file timely returns occurred despite the exercise of ordinary business care and prudence. (*Ibid.*) Appellant's arguments only show that it did not exercise care and prudence concerning its requirement to file tax returns with, and to pay tax to, a state in which it registered to do doing business (and was in fact doing enough business to meet the economic nexus standards for the tax years at issue). A reasonably prudent businessperson that registered to do business, and was actively engaged in business in California, would have, at the bare minimum, investigated California's tax requirements.³ Accordingly, appellant has not met its burden of establishing reasonable cause to abate the late filing penalties.

With regard to the per-shareholder late filing penalty, R&TC section 19172.5 provides that the penalty shall be imposed when an S corporation fails to file a tax return on or before the due date, unless it is shown that the failure is due to reasonable cause. Reasonable cause requires a showing that the taxpayer acted as an ordinarily intelligent and prudent businessperson would have acted under similar circumstances. (*Appeal of Quality Tax & Financial Services, Inc.,*

² See R&TC section 23101(b)(2)-(4) regarding economic nexus thresholds.

³ An S Corporation registered with the California SOS still has a filing requirement and owes the \$800 minimum franchise tax, even if it does not have economic nexus. (See R&TC, §§ 23802(c), 23153(a) & (b)(2).)

2018-OTA-130P.) Here, appellant presents the same arguments as it did for requesting abatement of the late filing penalties. However, as discussed above, appellant has not established reasonable cause and the per-shareholder late filing penalties cannot be abated.

HOLDING

Appellant has not established reasonable cause to abate the late filing penalties and the per-shareholder late filing penalties imposed for the 2014 through 2018 tax years.

DISPOSITION

FTB’s actions are sustained in full.

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Sara A. Hosey
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Sara A. Hosey
Administrative Law Judge

We concur:

DocuSigned by:
Kenneth Gast
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Kenneth Gast
Administrative Law Judge

DocuSigned by:
Lauren Katagihara
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Lauren Katagihara
Administrative Law Judge

Date Issued: 9/15/2023