

**OFFICE OF TAX APPEALS**  
**STATE OF CALIFORNIA**

In the Matter of the Appeal of:

**W. REDDEN AND**  
**S. REDDEN**

) OTA Case No. 220410238  
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**OPINION**

Representing the Parties:

For Appellants: Asia Smith, TAAP Student Representative<sup>1</sup>  
For Respondent: Vivian Ho, Attorney  
Maria Brosterhous, Attorney

M. Geary, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19324, W. Redden and S. Redden (appellants) appeal an action by the Franchise Tax Board (respondent) denying appellants’ claim for refund of a \$4,725 estimated tax penalty imposed by respondent for the 2019 tax year.

Appellants elected to have this appeal determined pursuant to the procedures of the Office of Tax Appeals’ (OTA’s) Small Case Program. Those procedures require the assignment of a single administrative law judge. (Cal. Code Regs., tit. 18, § 30209.05, et seq.) OTA Administrative Law Judge Michael F. Geary held a virtual (i.e., online) oral hearing for this matter on July 21, 2023. At the conclusion of the hearing, the parties submitted the matter and OTA closed the record.

**ISSUE**

Should the estimated tax penalty be abated?

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<sup>1</sup> The Tax Appeals Assistance Program provides free legal assistance to appellants in connection with appeals that meet certain requirements. The assistance is provided by law students who are supervised by tax counsel from respondent’s Taxpayers’ Rights Advocate’s Office.

FACTUAL FINDINGS

1. Appellants sold property on April 26, 2019, generating a substantial capital gain and resulting in a California adjusted gross income for the 2019 tax year in excess of \$1,000,000.
2. Appellants transferred a \$1,258 overpayment from 2018 to the 2019 tax year. They made estimated tax payments of \$1,110 on March 13, 2019, \$4,000 on June 10, 2019, and \$4,000 on October 8, 2020, and had income tax withheld of \$1,261 for the 2019 tax year. Their payments prior to the tax due date totaled \$11,629.
3. Respondent's form used by taxpayers who underpaid estimated taxes for the 2019 tax year (Form 5805) contained the following language at the top of the document:

**IMPORTANT:** In most cases, the Franchise Tax Board . . . can figure the penalty for you and you do not have to complete this form. See General Information B.

If you meet **any** of the following conditions, you do not owe a penalty for underpayment of estimated tax. **Do not complete or file this form if:**

- The amount of your tax liability (not including tax on lump-sum distributions and accumulation distribution of trusts) less credits (including the withholding credit) but not including estimated tax payments for either 2018 or 2019 was less than \$500 (or less than \$250 if married/RDP filing a separate return).
- Your 2018 return was for a full 12 months (or would have been if you were required to file) and you did not have any tax liability on that return.
- The amount of your withholding plus your estimated tax payments, **if paid in the required installments**, is at least 90 [percent] of the tax shown on your 2019 return or 100 [percent] of the tax shown on your 2018 return (110 [percent] if California adjusted gross income (AGI) was more than \$150,000 or \$75,000 if married/RDP filing a separate return) **and** you are not using the annualized income installment method. Taxpayers with California AGI equal to or greater than \$1,000,000 (or \$500,000 if married/RDP filing a separate return), must use the tax shown on their 2019 tax return if they do not meet one of the two conditions above.

(Bold print in original.)

4. Appellants timely filed their California Resident Income Tax Return on July 1, 2020, reporting a tax still due of \$144,404.<sup>2</sup>
5. Respondent imposed on appellants an estimated tax penalty of \$4,725.
6. Appellants paid the penalty and filed a claim for refund of the penalty.
7. Respondent denied the claim for refund. This timely appeal followed.

### DISCUSSION

Internal Revenue Code (IRC) section 6654 imposes an addition to tax, which is treated as and often referred to as a penalty, where taxpayers fail to timely pay estimated tax. The estimated tax penalty is similar to an interest charge in that it is calculated by applying the interest rate to the underpaid estimated tax. (See IRC, § 6654(a) [calculating estimated tax penalty by reference to the interest rate, established under IRC section 6621, imposed on underpayments]; R&TC, § 19136(b) [referring to R&TC section 19521 which, with modifications, conforms to the federal interest provisions in IRC section 6621]; *Appeal of Johnson*, 2018-OTA-119P.)

With some exceptions, R&TC section 19136 conforms to IRC section 6654 but modifies the due dates and amounts for payment of estimated taxes. As relevant to this appeal, one of the other ways in which R&TC section 19136 does not conform to IRC section 6654 is that IRC section 6654(d)(1)(B)(ii), the clause that allows a taxpayer a “safe harbor” of paying estimated taxes equal to 100 percent of the tax shown on the return of the individual for the preceding taxable year, does not apply if the adjusted gross income shown on the return of the individual for the taxable year is equal to or greater than \$1 million (\$500,000 in the case of a married individual filing a separate return). (R&TC, § 19136.3.) In other words, the law states clearly that the safe harbor of calculating estimated taxes based on the prior year’s tax return was not available to appellants.

There is no general reasonable cause exception to the estimated tax penalty. (*Appeal of Scanlon*, 2018-OTA-075P.) However, there are certain limited circumstances under which the estimated tax penalty will not apply. The exception upon which appellants rely provides that the penalty will not apply to the extent that, by reason of casualty, disaster, or other unusual

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<sup>2</sup> Due to the COVID-19 State of Emergency, FTB postponed the 2019 return due date from April 15, 2020, to July 15, 2020. (See <https://www.ftb.ca.gov/about-ftb/newsroom/news-releases/2020-3-state-postpones-tax-deadlines-until-july-15-due-to-the-covid-19-pandemic.html>.)

circumstances the imposition of such addition to tax would be against equity and good conscience.<sup>3</sup> (IRC, § 6654(e)(3).)

OTA has considered application of this exception before and found that the “unusual circumstances” referred to in the exception are considerably narrower than circumstances that would constitute reasonable cause. (*Appeal of Mazdyasni*, 2018-OTA-049P [citing IRS Field Service Advisory (Jun. 2, 1994) 1994 WL 1725487 (FSA)].) *Appeal of Mazdyasni, supra*, notes that the legislative history of IRC section 6654(e)(3)(A) “indicates that waiver may be appropriate where: the taxpayer’s books and records were destroyed by fire or other casualty; an estimated tax payment was not made due to the death or serious illness of the taxpayer; imposition of the penalty would be inequitable because, for example, the taxpayer substantially overstated their tax liability on their return or because the taxpayer designated that an overpayment of tax for the prior year be credited against their estimated tax, but the overpayment is offset for either past-due child support or non-tax federal debt under IRC section 6402 subdivision (c) or (d), and the taxpayer was not notified of the offset until after the due date for the estimated tax payment.” (Citing FSA, *supra*.; H.R. Conf. Rep. No. 861, 98th Cong., 2d Sess., 1115-1116 (1984); S. Rep. No. 169 (Vol 1) 98th Cong., 2d Sess. 506-507 (1984).)

Appellants argue that they are entitled to abatement of the penalty because the large increase in their income was the result of a once-in-a-lifetime event and because their failure to make timely and correct estimated tax payments was due to respondent’s poorly written, misleading, and confusing language at the top of the Form 5805, which caused them and their tax professional to not understand that their 2019 AGI in excess of \$1,000,000 prevented them from basing their estimated tax payments on their 2018 income.<sup>4</sup> More specifically, appellants claim that where the third bullet point states, “Taxpayers with California AGI equal to or greater than \$1,000,000 (or \$500,000 if married/RDP filing a separate return), must use the tax shown on their 2019 tax return if they do not meet one of the two conditions above,” appellants reasonably believed that the “two conditions above” referred to the two requirements set forth in the

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<sup>3</sup> The penalty also will not apply when the taxpayer retired after attaining the age of 62, or became disabled, during either the tax year under consideration of the immediately preceding tax year and the taxpayer establishes that the failure to timely pay the estimated tax payment was due to reasonable cause and not to willful neglect. Appellants have not argued or provided evidence to support application of this exception.

<sup>4</sup> Appellants at least imply that the subject language on Form 5805 for the 2019 tax year constituted the “instructions” for completion of the form. Respondent publishes separate instructions for its forms, which are available on FTB’s website. The full instructions for use of Form 5805 are not in evidence.

immediately preceding sentence. That sentence states, in essence, that the taxpayer does not owe a penalty and should not complete Form 5805 if the amount of the taxpayer's withholding plus estimated tax payments, if paid in the required installments, is at least 90 percent of the tax shown on the taxpayer's 2019 return or 100 percent of the tax shown on the taxpayer's 2018 return *and* the taxpayer was not using the annualized income installment method.

There is no dispute regarding the fact that appellants made inadequate estimated tax payments or that they were required by law to pay estimated taxes based on the tax amounts they expected to report on their 2019 return. The only question is whether appellants' once-in-a-lifetime increase in annual income or the language at the top of Form 5805 constitutes the kind of unusual circumstances that warrant relief.

Appellants' good fortune of having a substantial capital gain in April 2019 clearly did not prevent them from making the required estimated tax payments. It prevented appellants from calculating their estimated taxes based on the prior year's earnings, and it required a substantial increase in the payments due after the gain was realized, but these changes are no different than the ones faced by any taxpayer who has an unusual increase in their annual income. Such circumstances are not the kind of unusual circumstances upon which relief can be based. (See *Appeal of Saltzman*, 2019-OTA-070P [citing *Farhoumand v. Commissioner*, T.C. Memo. 2012-131].)

Turning now to the language on Form 5805, OTA notes that the obligation to pay estimated taxes does not arise from the language on a tax form. As explained above, it arises from the law, which clearly states that the safe harbor provision contained in IRC section 6654(d)(1)(B)(ii) does not apply if the adjusted gross income shown on the return of the individual for the taxable year is equal to or greater than \$1 million (\$500,000 in the case of a married individual filing a separate return). (R&TC, § 19136.3; IRC, § 6654(d)(1)(B)(ii).) Because the safe harbor provision was not available to appellants, they were required to base their estimated tax payments on 90 percent of the tax that will be shown on the return for the tax year for which the estimated payments are made. (R&TC, § 19136; IRC, § 6654(d)(1)(B)(i).) Had they done that, there would have been no penalty. Ignorance of the law is not reasonable cause for failure to comply with statutory requirements. (*Appeal of Porreca*, 2018-OTA-095P.) A taxpayer does not exercise ordinary business care and prudence when they fail to acquaint themselves with the requirements of California tax law. (*Ibid.*) On these bases, OTA finds that


appellants’ and their tax preparer’s claimed confusion regarding the language at the top of Form 5805 also do not constitute the kind of unusual circumstances upon which relief of the estimated tax penalty can be based.<sup>5</sup>

HOLDING

The estimated tax penalty should not be abated.

DISPOSITION

Respondent’s action denying appellants’ claim for refund is sustained.

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Michael F. Geary  
Administrative Law Judge

Date Issued: 10/5/2023

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<sup>5</sup> Although the above findings are dispositive, OTA also notes that the language at the top of Form 5805 clearly identifies each bulleted point as a “condition.” When the third bulleted point refers to “the two conditions above,” it is clearly referring to the first and second bulleted points. That interpretation is also consistent with the law.