

OFFICE OF TAX APPEALS
STATE OF CALIFORNIA

In the Matter of the Appeal of:
COMPNOVA LLC

) OTA Case No. 22039832
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OPINION

Representing the Parties:

For Appellant: Iram Rizvi, EA

For Respondent: Brian Werking, Attorney

E. LAM, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19324, Compnova LLC (appellant) appeals an action by respondent Franchise Tax Board (FTB) denying appellant’s claims for refunds in relation to various penalty amounts for the 2015 through 2019 tax years.¹

Appellant elected to have this appeal determined pursuant to the procedures of the Small Case Program. Those procedures require the assignment of a single administrative law judge. (Cal. Code Regs., tit. 18, § 30209.1.)

Office of Tax Appeals (OTA) Administrative Law Judge Eddy Y.H. Lam held an oral hearing for this matter electronically, on August 16, 2023. At the conclusion of the hearing, the record was closed and this matter was submitted for an opinion.

ISSUES

1. Whether appellant has established reasonable cause for the abatement of late payment of tax penalties imposed under R&TC section 19132 for the 2015 through 2019 tax years.
2. Whether appellant has established reasonable cause for the abatement of late filing penalties imposed under R&TC sections 19131 and 19172 for the 2019 tax year.

¹ The penalty amounts are indicated in the factual findings of this Opinion.

3. Whether appellant has established a legal basis to abate the underpayment of limited liability company (LLC) fee penalties imposed under R&TC section 17942(d)(2) for the 2016 through 2019 tax years.

FACTUAL FINDINGS

1. Appellant is a Texas LLC, registered to do business in California with the California Secretary of State on September 29, 2015.
2. In each of the tax years from 2015 through 2019, appellant filed the Partnership Return of Income (Form 565). However, since appellant is an LLC, it is instead required to file the LLC Return of Income (Form 568).
3. FTB issued a Request for Past Due LLC Return of Income (Request) for appellant's initial 2015 Form 568 because there were no records at the time to indicate that appellant filed Form 568.
4. Appellant did not respond to the Request; therefore, respondent sent a Demand to File an LLC Return (Demand) for the 2015 tax year. Since appellant did not respond to the Demand, FTB sent appellant a Final Notice Before Suspension or Forfeiture.
5. On October 1, 2019, FTB sent appellant a Notice of Suspension or Forfeiture because appellant did not file the correct Form 568 for the initial 2015 tax year.
6. On October 20, 2020, appellants untimely filed Form 568s for the tax years 2015 through 2019. Upon processing Form 568s, FTB assessed various penalties for each of the following tax years based on appellant's corrective filings:

2015 Tax Year

- On September 15, 2016, appellant incorrectly filed the 2015 Form 565, but later submitted the correct Form 568. On the 2015 Form 568, appellant reported a minimum tax of \$800 and an LLC fee of \$6,000.
- Upon processing the 2015 Form 568, FTB assessed a late payment penalty of \$1,563.

2016 Tax Year

- On September 15, 2017, appellant incorrectly filed the 2015 Form 565, but later submitted the correct 2017 Form 568. On the 2016 Form 568, appellant reported a minimum tax of \$800 and an LLC fee of \$6,000.

- Upon processing the 2016 Form 568, FTB assessed a late payment penalty of \$1,500, and an underpayment of estimated LLC fee penalty of \$600.

2017 Tax Year

- On September 17, 2018, appellant incorrectly filed the 2017 Form 565, but later submitted the correct Form 568. On the 2017 Form 568, appellant reported a minimum tax of \$800 and an LLC fee of \$6,000.
- Upon processing the 2017 Form 568, FTB assessed a late payment penalty of \$1,290, and an underpayment of estimated LLC fee penalty of \$600.

2018 Tax Year

- On September 16, 2019, appellant incorrectly filed the 2018 Form 565, but later submitted the correct Form 568. On the 2018 Form 568, appellant reported a minimum tax of \$800 and an LLC fee of \$6,000.
- Upon processing the 2018 Form 568, FTB assessed a late payment penalty of \$858, and an underpayment of estimated LLC fee penalty of \$520.

2019 Tax Return

- On September 15, 2020, appellant incorrectly filed the 2019 Form 565, but later submitted the correct Form 568. On the 2019 Form 568, appellant reported a minimum tax of \$800 and an LLC fee of \$2,500.
 - Upon processing the 2019 Form 568, FTB assessed a late payment penalty of \$38.50, an underpayment of estimated LLC fee penalty of \$250, a late filing penalty of \$250, and a per-partner late filing penalty of \$144.
7. After the penalties were paid in full, appellant filed claims for refund of all penalties, which FTB denied.
 8. This timely appeal followed.

DISCUSSION

Issue 1: Whether appellant has established reasonable cause for the abatement of late payment of tax penalties imposed under R&TC section 19132 for the 2015 through 2019 tax years.

R&TC section 19132 imposes a late payment penalty when a taxpayer fails to pay the amount shown as due on the return by the date prescribed for payment of that tax. The late payment penalty does not apply when the failure to pay is due to reasonable cause and not due to willful neglect. (R&TC, § 19132(a)(1).) The taxpayer bears the burden of proving “reasonable cause,” which means the taxpayer must show that its failure to pay the tax in a timely manner occurred despite the exercise of ordinary business care and prudence. (*Appeal of Moren*, 2019-OTA-176P.) Generally, a taxpayer’s reliance on an agent (such as an accountant or a tax attorney) to file a return or make timely payment of tax is not reasonable cause. (*United States v. Boyle* (1985) 469 U.S. 241 (*Boyle*)).

However, in *Boyle*, the U.S. Supreme Court held that “reasonable cause” is established when a taxpayer shows reasonable reliance on the advice of an accountant or attorney that it was unnecessary to file a return, even when such advice turned out to have been mistaken.² (*Boyle, supra*, at p. 250.) California follows *Boyle* in that a taxpayer’s reliance on a tax adviser must involve reliance on substantive tax advice and not on simple clerical duties. (*Appeal of Mauritzson*, 2021-OTA-198P, citing *Appeal of Berolzheimer* (86-SBE-172) 1986 WL 22860; *Appeal of Summit Hosting LLC*, 2021-OTA-216P.)

To establish reasonable cause under *Boyle*, a taxpayer must show it reasonably relied on a tax professional for substantive tax advice as to whether a tax liability exists and that the following conditions are met: (1) the person relied on by the taxpayer is a tax professional with competency in the subject tax law; and (2) the tax professional’s advice is based on the taxpayer’s full disclosure of relevant facts and documents. (*Boyle, supra*; *Appeal of Summit Hosting LLC, supra*.) By contrast, reliance on an expert cannot function as a substitute for compliance with an unambiguous statute. (*Boyle, supra*, at 251.) In *Appeal of Berolzheimer, supra*, Board of Equalization (BOE) found that there was no basis in the record for concluding that the New York law firm retained by taxpayers had expertise in California tax law. As a

² Decisions analyzing whether reasonable cause existed for failure to timely file a tax return are persuasive authority for determining whether reasonable cause existed for the failure to timely pay the tax. (*Appeal of Triple Crown Baseball LLC*, 2019-OTA-025P, at fn. 8.)

result, BOE declined to hold, as a matter of law, that relying on an out-of-state law firm could serve as reasonable cause for non-compliance with California’s tax laws.³

Here, appellant does not contest whether the late payment penalty was properly imposed or computed. Instead, appellant argues that the late payment for the 2015 through 2019 tax years was due to reasonable cause because it relied on the (incorrect) advice of a paid tax preparation firm for its California income tax filing obligations.

However, appellant’s assertions do not demonstrate reasonable cause for the late filing of its 2015 through 2019 returns. During oral hearing, the tax preparer indicated that the tax preparer is a Texas tax firm and has “very little” California tax filing knowledge. Statements made by appellant’s tax preparer show that the tax preparer does not regularly prepare California income tax returns or provide advice concerning California tax law. As such, similar to BOE’s holding in *Appeal of Berolzheimer, supra*, appellant’s reliance on an out-of-state tax preparer who lacks California tax expertise does not constitute reasonable cause for its non-compliance with California’s tax filing requirements and the resulting late payments. Thus, appellant has not met its burden of proof to abate late payment penalties for the 2015 through 2019 tax years under R&TC section 19132.

Issue 2: Whether appellant has established reasonable cause for the abatement of late filing penalties imposed under R&TC sections 19131 and 19172 for the 2019 tax year.

The R&TC contains two penalties that are applicable when an LLC classified as a partnership for tax purposes files its return late. First, R&TC section 19131 imposes a late filing penalty when a taxpayer fails to file its return on or before its due date, unless it is shown that the failure was due to reasonable cause and not willful neglect. The amount of the late filing penalty imposed by R&TC section 19131 is equal to five percent of the tax and LLC fee due after allowing for timely payments, for every month or fraction of a month the return is late, not to exceed 25 percent of the tax due. (R&TC, §§ 19131(a), 17942(c).)

A second penalty, imposed under R&TC section 19172 takes into account the fact that an LLC classified as a partnership is a pass-through entity. R&TC section 19172 imposes a per-partner, late-filing penalty when a partnership—or an LLC classified as a partnership—fails to

³ California Code of Regulations, title 18, section 30504, provides that precedential opinions of BOE that were adopted prior to January 1, 2018, may be cited as precedential authority to OTA unless a panel removes, in whole or in part, the precedential status of the opinion.

file a return at the time prescribed unless it is shown that the failure was due to reasonable cause. The amount of the per-partner, late filing penalty under R&TC section 19172 is computed by multiplying \$18 by the number of partners by the number of months, or fraction thereof, that the return is late (not to exceed 12 months). (R&TC, 19172(a)(2).)

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 ordinar[ily] intelligent and prudent business[person] to have so acted under similar circumstances.” (*Appeal of GEF Operating, Inc.*, 2020-OTA-057P.) Ignorance of a filing requirement or a misunderstanding of the law generally does not excuse a late filing. (*Ibid.*)

Appellant does not contest whether the late filing penalty was properly imposed or computed.⁴ Rather, appellant asserts the same reasonable cause argument with regards to abating the late payment penalty because it relied on the (incorrect) advice of a paid tax preparation firm regarding its California income tax filing obligations.

As stated above, reasonable cause did not exist because appellant’s reliance on an out-of-state tax preparer who lacks California tax expertise does not constitute reasonable cause for its non-compliance with California's tax filing requirements.⁵ (*Appeal of Berolzheimer, supra.*) Thus, appellant has not met its burden of proof to abate the late filing penalties imposed for the 2019 tax year under R&TC sections 19131 and 19172.

⁴ FTB did not impose the late filing penalties for tax years 2015 through 2018 because of the receipt of appellant’s incorrect Form 565s by the seven-month automatic extension due date. However, appellant’s LLC status was forfeited on October 1, 2019. Accordingly, unlike appellant’s previous tax years, a forfeited entity is not entitled to the seven-month automatic extension. Therefore, appellant’s 2019 Form 565 filed on September 15, 2020, was filed late. The original due date for filing the 2019 tax return is on April 15, 2020, which was postponed to July 15, 2020, due to COVID-19 pandemic. (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> .)

⁵ The issue of whether a taxpayer has demonstrated reasonable cause for failure to pay tax asks the same questions and weighs the same evidence as the inquiry of whether reasonable cause exists for failure to file a tax return. (See *Appeal of Triple Crown Baseball LLC, supra*, at fn. 8.)

Issue 3: Whether appellant has established a legal basis to abate the underpayment of LLC fee penalties imposed under R&TC section 17942(d)(2) for the 2016 through 2019 tax years.

R&TC section 17942 imposes an LLC fee based on total California source income of LLCs that are doing business in California. The LLC fee is required to be estimated and paid on or before the 15th day of the sixth month of the current taxable year. (R&TC, § 17942(d)(1).) When the estimated payment of the LLC fee is less than the amount of the LLC fee due for the taxable year, a penalty equal to 10 percent of the underpayment is imposed unless the fee amount that was timely estimated and paid was equal to or greater than the total amount of the LLC fee for the preceding taxable year. (R&TC, § 17942(d)(2).) If the estimated LLC fee is not paid on time, a penalty of 10 percent of the amount of the underpayment is added to the fee. (*Ibid.*) The statute does not provide for a reasonable cause exception to the imposition of the penalty. (*Ibid.*) The only defense authorized by statute is the safe harbor provision, which provides that the penalty will not be imposed if the estimated LLC fee that is timely paid is equal to or exceeds the LLC fee due for the prior tax year. (*Ibid.*; *Appeal of Summit Hosting LLC, supra.*)

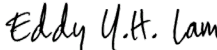
Appellant does not contest whether the underpayment of LLC fee penalties were properly imposed or computed. Rather, appellant appears to assert that reasonable cause exists to abate the underpayment of LLC fee penalties. However, as noted above, the R&TC does not contain a reasonable cause or extenuating circumstances exception to the underpayment of LLC fee penalties imposed on a taxpayer. (See *Appeal of Summit Hosting LLC, supra.*) Here, there is no basis for abatement of the underpayment of LLC fee penalties. Therefore, appellant has not met its burden of proof to abate the underpayment of LLC fee penalties imposed for the 2016 through 2019 tax years under R&TC section 17942(d)(2).

HOLDINGS

1. Appellant has not established reasonable cause for the abatement of late payment of tax penalties imposed under R&TC section 19132 for the 2015 through 2019 tax years.
2. Appellant has not established reasonable cause for the abatement of late filing penalties imposed under R&TC sections 19131 and 19172 for the 2019 tax year.
3. Appellant has not established a legal basis to abate the underpayment of LLC fee penalties imposed under R&TC section 17942(d)(2) for the 2016 through 2019 tax years.

DISPOSITION

FTB's denial of appellant's claims for refund are sustained.

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Eddy Y.H. Lam
Administrative Law Judge

Date Issued: 11/7/2023