

BEFORE THE OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

IN THE MATTER OF THE APPEAL OF,)
)
E.J. LAWLESS and C. LAWLESS,) OTA NO. 220710731
)
 APPELLANT.)
)
)

TRANSCRIPT OF ELECTRONIC PROCEEDINGS

State of California

Thursday, December 14, 2023

Reported by:
ERNALYN M. ALONZO
HEARING REPORTER

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E.J. LAWLESS and C. LAWLESS,) OTA NO. 220710731
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Transcript of Electronic Proceedings,
taken in the State of California, commencing
at 2:09 p.m. and concluding at 2:31 p.m. on
Thursday, December 14, 2023, reported by
Ernalyn M. Alonzo, Hearing Reporter, in and
for the State of California.

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APPEARANCES:

Panel Lead: ALJ KEITH LONG

Panel Members: ALJ LAUREN KATAGIHARA
ALJ TERESA STANLEY

For the Appellant: JAMES FIELDING

For the Respondent: STATE OF CALIFORNIA
FRANCHISE TAX BOARD
ERIC BROWN
CYNTHIA KENT

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I N D E X

E X H I B I T S

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California; Thursday, December 14, 2023
2:09 p.m.

JUDGE LONG: We're opening the record in the Appeal of Lawless. OTA Case No. is 220710731. This matter is being held before the Office of Tax Appeals. Today's date is Thursday, December 14th, 2023, and the time is 2:09 p.m. This hearing is being convened electronically.

Today's hearing is being heard by a panel of three Administrative Law Judges. My name is Keith Long, and I will be the lead Administrative Law Judge. Judge Teresa Stanley and Judge Lauren Katagihara are the other members of this tax appeals panel. All three judges will meet after the hearing and produce a written decision as equal participants. Although the lead judge will conduct the hearing, any judge on this panel may ask questions or otherwise participate to ensure that we have all the information needed to decide this appeal.

Also present is a stenographer, Ms. Alonzo, who is reporting this hearing verbatim. To ensure we have an accurate record, we ask that everyone speaks one at a time and does not speak over each other. Also, speak clearly and loudly. When needed, Ms. Alonzo will stop the hearing process and ask for clarification. After the hearing,

1 Ms. Alonzo will produce the official hearing transcript,
2 which will be available on the Office of Tax Appeals
3 website.

4 The Office of Tax Appeals is an independent and
5 neutral agency. It is not a Tax Court. All three judges
6 are co-equal decision makers, and we can all ask questions
7 at any time.

8 I'd like to offer a few reminders to help the
9 process run as smoothly as possible. Please ensure your
10 microphone is not muted when you speak otherwise, your
11 voice will not be picked up on the live stream. Please
12 mute your microphones when you are not speaking to avoid
13 feedback and other interferences. As a reminder, these
14 proceedings are being broadcast live, so anything said
15 today and any information shared today is publicly
16 viewable on the live stream.

17 For the record, will the parties please state
18 their names and who they represent, starting with the
19 representatives for Appellant.

20 MR. FIELDING: James Fielding.

21 JUDGE LONG: Thank you.

22 And for Franchise Tax Board.

23 MR. BROWN: Eric Brown, Tax Counsel, Franchise
24 Tax Board.

25 MS. KENT: Cynthia Kent with the Franchise Tax

1 Board.

2 JUDGE LONG: Okay. Thank you.

3 At the prehearing conference, Appellants and FTB
4 each indicated that there would be no witness testimony.

5 Mr. Fielding, is that correct?

6 MR. FIELDING: Correct.

7 JUDGE LONG: And, Franchise Tax Board, is that
8 correct?

9 MR. BROWN: That is correct.

10 JUDGE LONG: Thank you.

11 At the prehearing conference, OTA identified FTB
12 Exhibits A through F. There were no objections to FTB's
13 exhibits at that time.

14 Can Appellant please confirm whether there are
15 any objections at this time.

16 MR. FIELDING: There are no objections.

17 JUDGE LONG: Thank you.

18 FTB's exhibits are admitted in this hearing.

19 (Department's Exhibits A-F were received in
20 evidence by the Administrative Law Judge.)

21 JUDGE LONG: There are no other exhibits for this
22 oral hearing.

23 There is one issue in this appeal. It is whether
24 Appellants have established reasonable cause for their
25 late payment of tax.

1 At the prehearing conference, Appellant requested
2 10 minutes to make their presentation.

3 Mr. Fielding, you may begin when ready.

4 MR. FIELDING: Thank you.

5

6 PRESENTATION

7 MR. FIELDING: Thank you for the opportunity to
8 speak here today.

9 The Appellants, the Lawlesses, first came to
10 California and became California residents and taxpayers
11 in 2017. The Appellants have consistently timely filed
12 California personal income tax returns and timely paid
13 California personal income tax, present matter excluded.
14 Appellants have been in good-faith compliance with
15 California personal income tax rules and the filing and
16 tax payment requirements. There has been an absence of
17 willful neglect in the Appellants' California personal
18 income tax obligations. But, generally, the principle
19 portion of the applicants' California personal income tax
20 has been paid by employer state income tax withholding.

21 For -- once an accurate determination of the
22 Appellants' California personal income tax for 2022 was
23 computed, they were surprised to learn that their 2022 --
24 excuse me. I mean, 2020 -- surprise to learn that their
25 2020 income tax was more than \$328,000 in total. After

1 actual state income tax withholding of \$190,000,
2 approximately, the amount of tax due with the 2020
3 Form 540 was \$139,000, rounding amounts for small
4 differences. Surprised -- they were surprised because the
5 applicants' state income tax withholding covered most, if
6 not all, of their annual state income taxes in previous
7 years and, in fact, respectively.

8 Appellants properly determined that they can pay
9 the state \$25,000 from cash on hand with the filing of an
10 extension, but they would have to liquidate certain stocks
11 and mutual funds in order to pay -- in order to provide
12 the liquidity to pay the remaining California tax due of
13 approximately \$114,000 without penalty and interest.
14 Appellants arranged for the proper payment of the balance
15 due and paid the balance due with the timely filed
16 extension -- timely filed on extension, California
17 personal tax return on or before May 25th, 2021.

18 Accordingly, the balance of the state income tax
19 was paid within eight days of the original due date. The
20 Appellants' temporary illiquidity was an isolated
21 occurrence as is evidenced by the fact that a similar
22 liquidity -- illiquidity has not reoccurred in the
23 post-2020 personal income tax filings. Appellants have
24 timely filed and paid their California personal income
25 taxes in their 2021 and 2022 tax filings.

1 Now, we understand the income tax system is one
2 of voluntary compliance with the tax laws. Penalties may
3 be in the law to encourage compliance on the voluntary
4 nature of the system. However, in this instance, the
5 \$6,000 late-payment penalty appears egregious and
6 excessive under the circumstances whereby there was no
7 willful neglect nor intent not to comply with the
8 California personal income tax rules.

9 Now, as we previously mentioned in the
10 Appellants' response to Respondent's opening brief, that
11 the State may waive penalties where the failure to comply
12 was not due to willful neglect or intent not to comply,
13 section 21015 of the rules and Tax Code. Now, Respondent
14 summarily dismissed the reference section as it was not
15 applicable to personal income taxes. However, we believe
16 section 21015 was cited by analogy as a provision included
17 in the State's law expressing a willingness to dismiss
18 penalties when there are willful neglect or intent not to
19 comply on the part of taxpayers.

20 And as a last statement, we note that the State
21 has fully revised at the end of 2022 R&TC section 19132.5
22 to provide for first time penalty abatement, which may
23 have been reasonably applied to the situation like this
24 instance. Although the revised section will not apply
25 today, it demonstrates the intent of the State to more

1 reasonably deal with taxpayers in the future.

2 That completes my statement.

3 JUDGE LONG: Thank you, Mr. Fielding. I do have
4 maybe a few questions. With respect to the income tax
5 liability for 2020, the surprise amount, was there an
6 unexpected change in the taxpayer's income during that
7 year that would have caused that to be a surprise?

8 MR. FIELDING: Now, I will be talking off the top
9 of my head without going back and taking a look at their
10 return, but yes. As I recall, a liquidity event in one of
11 the taxpayer's primary employers. They -- she, Claire,
12 Mrs. Lawless, received extra income that was unusual.

13 JUDGE LONG: And my understanding from the return
14 is that most of the income received that year was W-2 wage
15 income. Was that unusual income included in that, or was
16 it the addition that was not W-2 income?

17 MR. FIELDING: As I understand it, it was
18 unusual. It was compensatory, and that's why it was
19 included in the W-2. And, frankly, I'm not even sure it
20 was all cash.

21 JUDGE LONG: Okay. And so is there any
22 explanation for why amounts of additional income wouldn't
23 have withholding?

24 MR. FIELDING: Would have a what, sir?

25 JUDGE LONG: Wouldn't have additional

1 withholdings?

2 MR. FIELDING: I can't say for sure what the
3 employer was doing. I don't know right now without going
4 back through our 2020 files if that income was all cash
5 income. It could have been some type of stock that was
6 triggered to Mrs. Lawless upon the liquidity event of a
7 corporation in which she was invested as an employee.

8 JUDGE LONG: And then, with respect to the
9 additional income, was there any reason that Appellants
10 wouldn't have been able to ascertain that they owed
11 additional income -- or sorry -- would have a larger
12 income tax liability based on that surprise income prior
13 to the due date for payment?

14 MR. FIELDING: I would be -- I mean, I can't tell
15 for sure.

16 JUDGE LONG: Okay.

17 MR. FIELDING: I believe, as I said in my
18 statement, that they believe that there was enough income
19 tax withholding since there always had been enough income
20 tax withholding to pay the tax that would be due.

21 JUDGE LONG: Right. Thank you. I don't have any
22 additional questions.

23 I would like to turn to my co-Panelists to see if
24 they have any questions this afternoon.

25 Judge Stanley, do you have any questions?

1 JUDGE STANLEY: This is Judge Stanley. I don't
2 have any follow-up questions. I think that most of my
3 questions were answered in the last round. So, thank you.

4 JUDGE LONG: Thank you.

5 And, Judge Katagihara, do you have any questions?

6 JUDGE KATAGIHARA: No questions at this time.

7 Thank you.

8 JUDGE LONG: Okay. At this time, I would like to
9 turn to Franchise Tax Board.

10 Franchise Tax Board, you have 10 minutes to make
11 your presentation, and you may begin when you are ready.

12 MR. BROWN: Thank you.

13

14 PRESENTATION

15 MR. BROWN: Good afternoon. I'm Eric Brown, Tax
16 Counsel with the Franchise Tax Board. As you can tell I
17 have a cold, so I'm doing the best I can. But anyhow,
18 also appearing with me is Cynthia Kent.

19 In the present appeal, excuse me, Appellants have
20 failed to show reasonable cause to abate the late-payment
21 penalty for the 2020 tax year. Appellants filed their
22 2020 California tax return on May 25, 2021, eight days
23 after the original due date for tax year 2020, but within
24 the automatic filing extension deadline. They reported a
25 balance due of \$113,743 and remitted a payment in that

1 amount along with their return.

2 Thereafter, Respondent imposed the late-payment
3 penalty, which Appellants paid and then filed their claim
4 for refund, which Respondent denied. On appeal,
5 Appellants argue they were unable to pay the balance on
6 the due date because of financial inability which required
7 liquidation of investment assets. Appellants provide no
8 facts or argument about the need to liquidate assets to
9 pay their tax, nor why they were not in a financial
10 position to make a timely tax payment in the first place.

11 As discussed, Respondent's brief, over 90 percent
12 of Appellants' taxable income is attributable to wages
13 reported in federal forms W-2, which are required by law
14 to be provided to employees by employers before
15 January 31st, following the close of the taxable year.
16 Yet. Appellants' unpaid balance was 35 percent of the
17 total tax due. Respondent also notes that in the first
18 quarter of 2021 Appellants received over \$395,000 in wages
19 from their respective employers. Appellants provide no
20 explanation for why they failed to plan to make timely tax
21 payments, nor did they argue why they have established
22 reasonable cause to abate the penalty. Accordingly,
23 Respondent's denial of Appellants' claim for refund should
24 be sustained.

25 I would be happy to respond to any questions the

1 Panel may have.

2 JUDGE LONG: Thank you. I do have one question
3 for Franchise Tax Board. So at the time of filing, the
4 filing date was eight days after the due date of the
5 return, but within the automatic extension period. At
6 that point, the -- sorry. Let me try and rephrase this.

7 The due date for payment wasn't extended; that is
8 correct?

9 MR. BROWN: That is correct, Judge.

10 JUDGE LONG: Okay. So at the time of filing, the
11 payment would already have been late in FTB's estimation
12 or position?

13 MR. BROWN: Yes. And that's statutory language
14 that an extension to file is not an extension to pay.

15 JUDGE LONG: Okay. Thank you.

16 Judge Stanley, do you have any questions?

17 JUDGE STANLEY: This is Judge Stanley. No, I
18 don't have any questions for the Franchise Tax Board.
19 Thank you.

20 JUDGE LONG: Thank you.

21 And, Judge Katagihara, do you have any questions?

22 JUDGE KATAGIHARA: No questions.

23 JUDGE LONG: Okay. Well, then I believe,
24 Mr. Fielding, we are ready for your closing statement.
25 You have 10 minutes, and you may begin when you are ready.

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10 If that factual part of this equation becomes
11 critical, I can certainly determine what happened and
12 provide an answer. But absent that, we still believe that
13 the late-payment penalty, it just is excessive in a
14 situation where you have taxpayers who have complied in
15 good faith with the tax laws and happen to be caught in an
16 isolated occurrence of illiquidity to pay their full taxes
17 when the due date came.

19 JUDGE LONG: Okay. Thank you.

22 | Are we ready to --

24 JUDGE LONG: Yes. Go ahead.

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1 response, there is no evidence that there were any stock
2 options or deferred, kind of, compensation that is in the
3 record nor that was in the returns. Secondly, the
4 facts -- any such facts would have been available prior to
5 prehearing conference, and they have not been introduced.
6 So we object on those grounds.

7 JUDGE LONG: Okay. Thank you.

8 Okay. I'm going to give Appellants one last
9 opportunity to respond to Mr. Brown. And I agree, I don't
10 think any additional documentation is needed at this time.

11 But, Mr. Fielding, if you would like to respond,
12 please do so.

13 MR. FIELDING: Well, I don't agree with Mr. Brown
14 that there wouldn't be -- I will agree with the statement
15 that no evidence has been presented that the compensation
16 of a large amount was non-cash, but there wouldn't be in
17 the ordinary course of events in preparing a tax return.
18 So that evidence would have to be supplemental to the tax
19 return.

20 JUDGE LONG: Okay. I understand.

21 All right. And my co-Panelists have indicated
22 that they do not have any questions. So we are going to
23 conclude this hearing.

24 This case is submitted on Thursday,
25 December 14th, 2023.

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I want to thank everyone for calling in today.
The ALJs will meet and decide your case later on, and we
will send you a written opinion of our decision within
100 days from today.

Today's hearing in the Appeal of Lawless is now
adjourned.

This concludes our calendar for 2023. Thank you.

(Proceedings adjourned at 2:31 p.m.)

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HEARING REPORTER'S CERTIFICATE

I, Ernalyne M. Alonzo, Hearing Reporter in and for
the State of California, do hereby certify:

That the foregoing transcript of proceedings was
taken before me at the time and place set forth, that the
testimony and proceedings were reported stenographically
by me and later transcribed by computer-aided
transcription under my direction and supervision, that the
foregoing is a true record of the testimony and
proceedings taken at that time.

I further certify that I am in no way interested
in the outcome of said action.

I have hereunto subscribed my name this 12th day
of January, 2024.

ERNALYN M. ALONZO
HEARING REPORTER