

**OFFICE OF TAX APPEALS
STATE OF CALIFORNIA**

In the Matter of the Appeal of:) OTA Case No. 230413027
D. WEST AND)
M. WEST)
_____)

OPINION

Representing the Parties:

For Appellants: Hugh A. Moran, CPA

For Respondent: Christopher T. Tuttle, Attorney

S. HOSEY, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19324, D. West and M. West (appellants) appeal an action by respondent Franchise Tax Board (FTB) denying appellants' claims for refund of \$26,239 for the 2019 tax year, and \$2,333 plus interest for the 2021 tax year.

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

ISSUES

1. Whether appellants are entitled to abatement of the underpayment of estimated tax penalty (estimated tax penalty) for the 2019 and 2021 tax years.
2. Whether appellants are entitled to interest abatement for the 2021 tax year.

FACTUAL FINDINGS

1. Appellants timely filed their joint 2019 California income tax return reporting taxable income of \$8,218,616 and total tax of \$1,052,601. After reporting withholding credits and estimated tax payments, appellants determined they had an overpayment, which they opted to be applied as an estimated tax payment for the 2020 tax year.
2. FTB processed the 2019 return and applied an estimated tax penalty of \$26,239 because appellants did not timely make their installments of the required annual payment.

3. Appellant submitted a claim for refund arguing their payment was timely under the COVID-19 extended deadline and therefore the estimated tax penalty should be abated.
4. FTB applied the remaining credit on the 2019 tax year of \$195,041 to tax year 2020, with an effective date of April 15, 2020, but did not abate the estimated tax penalty for 2019.
5. Appellants timely filed their joint 2021 California income tax return reporting taxable income of \$2,907,819 and total tax of \$344,479. After reporting \$362,529 in estimated tax payments, appellants determined they had an overpayment, which they opted to be applied as an estimated tax payment for the 2022 tax year.
6. FTB processed the 2021 tax return and applied an estimated tax penalty of \$2,333 because appellants did not timely make their installments of the required annual payment.
7. FTB sent appellants a Notice of Tax Return Change – Revised Balance for tax year 2021, which informed appellants that the difference between the estimated tax payments reported by appellants (\$362,529) and the amount received (\$336,290) equals the \$26,239 amount of the estimated tax penalty appellants believed should have been refunded to them from tax year 2019 (and applied to tax year 2021).
8. Appellants sent a letter to FTB arguing that the 2019 penalty should be abated and that the resulting credit should be refunded. Appellants failed to pay the balance due and FTB issued collection notices for the 2021 tax year. Appellants subsequently paid the full balance due.
9. FTB denied appellants' claims for refund because they had not established grounds for abatement of the estimated tax penalties for the 2019 and 2021 tax years, or abatement of interest for the 2021 tax year.
10. This timely appeal followed.

DISCUSSION

Issue 1: Whether appellants are entitled to abatement of the estimated tax penalty for the 2019 and 2021 tax years.

Except as otherwise provided, R&TC section 19136 conforms to Internal Revenue Code (IRC) section 6654 and imposes an addition to tax, which is treated as and often referred to as a

penalty, where taxpayers fail to timely pay estimated tax.¹ The estimated tax penalty is similar to an interest charge in that it is calculated by applying the applicable interest rate to the underpaid estimated tax. (See IRC, § 6654(a); R&TC, § 19136(b); *Appeal of Johnson*, 2018-OTA-119P.)

For the 2019 and 2021 tax years, appellants' adjusted gross income (AGI) exceeded \$1 million and therefore the required annual payment was 90 percent of the tax shown on the current year return. (R&TC, § 19136.3.) Appellants' 2019 required annual payment was \$947,340.90 (\$1,052,601 x 0.90) and their 2021 required annual payment was \$310,031.10 (\$344,479 x 0.90). For the 2019 tax year, appellants required annual payment was to be paid accordingly: \$278,237.97 on April 15, 2019; \$370,983.96 on June 15, 2019; and \$278,237.97 on January 15, 2020.² For tax year 2021, appellants required annual payment was to be paid accordingly: \$93,009.33 on April 15, 2021; \$124,012.44 on June 15, 2021; and \$93,009.33 on January 15, 2022.³ The annual payments for both tax years were vastly underpaid as, by the end of 2019, only approximately \$76,000 in timely payments were made, whereas approximately \$940,000 was required.⁴ For tax year 2021, the parties concede that the difference between the estimated tax payments reported by appellants (\$362,529) and the amount received (\$336,290) equals the \$26,239 amount of the estimated tax penalty appellants believed should have been refunded to them and applied as an estimated tax payment from tax year 2019. Appellants failed to timely make the required annual payments in full for the 2019 and 2021 tax years; therefore, FTB properly imposed estimated tax penalties on the underpayments.

Appellants do not contest the imposition or computation of the estimated tax penalty for either tax year. Instead, appellants argue that the safe harbor rule should qualify them for abatement of the estimated tax penalty. While IRC section 6654(d)(1)(B)(ii) provides the safe harbor rule, it does not apply for California purposes if the taxpayer's AGI for the current year is equal to or greater than \$1 million. (R&TC, § 19136.3.) As appellants' AGI exceeds \$1 million

¹ Where estimated tax payments are due, R&TC section 19136.1(a)(2) generally requires, for California income tax purposes, that the payments be made in installments on or prior to April 15 and June 15 of the applicable tax year, and January 15 of the subsequent tax year. For federal income tax purposes, an additional installment is also due by September 15 of the applicable tax year. (IRC, § 6654.)

² These amounts are the amounts due after application of withholding credits.

³ These amounts are the amounts due after application of withholding credits.

⁴ While appellants argue that the July 15, 2020 payment of \$1,000,000 for the 2019 tax year fell under the extended COVID-19 payment deadlines, the FTB release states that only 1st and 2nd quarter estimate payments for tax year 2020 were extended (not those for tax year 2019).

for both applicable tax years; therefore, the safe harbor rule does not apply to either tax year.

Appellants also argue that the underpayment was due to reasonable cause, because of their age and retirement in 2019, not willful neglect. They also state they have good payment history. 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-079P.) As a result, there is no general reasonable cause exception to the imposition of the estimated tax penalty, and the estimated tax penalty imposed under IRC section 6654 is mandatory unless taxpayers establish that a statutory exception applies. (*Ibid.*; *Appeal of Scanlon*, 2018-OTA-075P.) IRC section 6654(e)(3)(A) provides that the taxing agency may waive the estimated tax penalty if it determines that “by reason of casualty, disaster, or other unusual circumstances the imposition of [the estimated tax penalty] would be against equity and good conscience.” The exception for unusual circumstances is considerably narrower than reasonable cause. (*Appeal of Mazdyasni*, 2018-OTA-049P.) Appellants do not allege that they were subject to unusual circumstances, only that they mistakenly thought they were subject to the safe harbor rule since they were retired.

IRC section 6654(e)(3)(B) provides that FTB may waive the estimated penalty where it determines that (i) during the tax year for which the estimated payments were required to be made, or the preceding year, the taxpayer either retired after having attained age 62, or became disabled, and (ii) the underpayment was due to reasonable cause and not willful neglect.

Although there is no guidance as to what constitutes reasonable cause for purposes of IRC section 6654(e)(3)(B), the same standard applies to other penalties, and the Office of Tax Appeals (OTA) looks to cases involving those penalties for guidance. To establish reasonable cause, a taxpayer must show that their failure to make a timely tax payment of the proper amount occurred despite exercising ordinary business care and prudence. (See *Appeal of Friedman*, 2018-OTA-077P; *Appeal of Scanlon*, 2018-OTA-075P.) The taxpayer bears the burden of proving that an ordinarily intelligent and prudent businessperson would have acted similarly under the circumstances. (*Ibid.*) The failure, caused by an oversight, to timely remit the balance due on a tax liability does not, by itself, constitute reasonable cause. (See *Appeal of Risser* (84-SBE-044) 1984 WL 16123 [relating to timely payment of tax].)

Appellants allege D. West was 71 when he retired in 2019 and M. West was 63 when she retired in 2019. Even if OTA had been provided with supporting documentation for these

assertions, appellants have not shown that the underpayment was due to reasonable cause. Appellants argue that the underpayment was due to their age and retirement. While OTA is sympathetic to appellants' situation, ignorance of the law does not excuse noncompliance with statutory requirements. (*Appeal of Diebold, Inc.* (83-SBE-002) 1983 WL 15389.) The 2019 Instructions for Form 540-ES, Estimated Tax for Individuals,⁵ provides, "Taxpayers with 2019 California adjusted gross income equal to or greater than \$1,000,000 ... must figure estimated tax based on their tax for 2019." Based on the availability of these instructions to all taxpayers, appellants could be reasonably expected to know of the requirement for the payment of estimated tax for individuals who had California AGI equal to or greater than \$1 million.

Moreover, appellants have not described what efforts, if any, they took to ensure that they timely paid the correct amount of estimated tax payments. The events, as presented by appellants, do not show that the underpayment of estimated taxes occurred despite the exercise of ordinary business care and prudence. Appellants have not explained their efforts to ensure the tax was timely paid. Additionally, appellants' statements regarding their history of timely payment and that they did not intend to pay late are not relevant to waiver under IRC section 6654(e)(3)(B). (*Appeal of Mazdyasni, supra*; *Appeal of Saltzman, supra*.)

As described above, the estimated tax penalty is similar to an interest charge and compensates the government for the time value of the tax that is due but not paid until a later date. OTA does not consider the estimated tax penalty to be imposed improperly under appellants' circumstances. Thus, the estimated tax penalty may not be waived or abated.

Issue 2: Whether appellants are entitled to interest abatement for the 2021 tax year.

Interest must be assessed from the date a tax payment is due through the date that it is paid. (R&TC, § 19101.) Imposing interest is mandatory; it is not a penalty, but it is compensation for appellants' use of money after it should have been paid to the state. (*Appeal of Moy*, 2019-OTA-057P.) Generally, to obtain relief from interest, taxpayers must qualify under

⁵ <https://www.ftb.ca.gov/forms/2019/2019-540-es-instructions.html>.

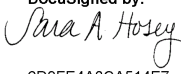
R&TC section 19104, 19112, or 2012.⁶ (*Ibid.*) Appellants do not allege that any of the three statutory provisions for interest abatement apply to the facts of this case, and OTA concludes based on the written record that none of these statutory provisions apply. Therefore, FTB properly imposed interest and OTA has no basis to abate it.

HOLDINGS


1. Appellants are not entitled to abatement of the estimated tax penalty for the 2019 and 2021 tax years.
2. Appellants are not entitled to interest abatement for the 2021 tax year.


DISPOSITION

FTB's actions are sustained.

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 Sara A. Hosey
 Administrative Law Judge

We concur:

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 Amanda Vassigh
 Administrative Law Judge

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 Asaf Kletter
 Administrative Law Judge

Date Issued: 11/15/2023

⁶ Under R&TC section 19104, FTB is authorized to abate or refund interest if there has been an unreasonable error or delay in the performance of a ministerial or managerial act by an FTB employee. Under R&TC section 19112, FTB may waive interest for any period for which FTB determines that an individual has extreme financial hardship. OTA does not have authority to review extreme financial hardship determinations. (See *Appeal of Moy, supra.*) Under R&TC section 21012, an individual may be relieved from interest if that person reasonably relies on FTB's written advice in response to a written request.