

**OFFICE OF TAX APPEALS
STATE OF CALIFORNIA**

In the Matter of the Appeal of:) OTA Case No. 220710731
E. LAWLESS AND)
C. LAWLESS)
_____)

OPINION

Representing the Parties:

For Appellants: James J. Fielding, CPA

For Respondent: Eric R. Brown, Attorney
Cynthia D. Kent, Attorney

K. LONG, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19324, E. Lawless and C. Lawless (appellants) appeal an action by respondent Franchise Tax Board (FTB) denying appellants’ claim for refund of \$6,255.87 for the 2020 tax year.

Office of Tax Appeals (OTA) Administrative Law Judges Lauren Katagihara, Teresa A. Stanley, and Keith T. Long held an oral hearing electronically for this matter on December 14, 2023. At the conclusion of the hearing, the record was closed, and this matter was submitted for an opinion.

ISSUE

Whether appellants have established reasonable cause for the late payment of their 2020 tax liability.

FACTUAL FINDINGS

1. Appellants filed a timely joint California resident income tax return. After applying withholding credits of \$189,408 and an extension payment of \$25,000, appellants reported a tax due of \$113,743. On May 25, 2021, appellants made an untimely payment of \$113,743, satisfying their tax liability.

2. FTB imposed a late payment penalty of \$6,255.87, and applicable interest.¹
3. Appellants filed a claim for refund asserting that there was reasonable cause for the late payment of tax.²
4. On October 20, 2021, appellants made a payment of \$6,331.55, satisfying the liability.
5. On April 15, 2022, FTB denied appellants' claim for refund of the late payment penalty.
6. This timely appeal followed.

DISCUSSION

R&TC section 19132 imposes a late payment penalty when taxpayers fail to pay the amount shown as due on the return by the date prescribed for the payment of tax. Generally, the date prescribed for the payment of the tax is the due date of the return (without regard to extensions of time for filing). (R&TC, § 19001.) The late payment penalty is comprised of two parts. The first part is 5 percent of the unpaid tax. (R&TC, § 19132(a)(2)(A).) The second part is 0.5 percent of the unpaid tax, per month or a portion thereof, not to exceed 40 months. (R&TC, § 19132(a)(2)(B).)

When FTB imposes a penalty, it is presumed that the penalty was imposed correctly. (*Appeal of Xie*, 2018-OTA-076P.) However, the late payment penalty may be abated if the taxpayers show that the failure to make a timely payment of tax was due to reasonable cause and was not due to willful neglect. (R&TC, § 19132(a)(1).) FTB does not argue that appellants acted with willful neglect. Thus, to establish reasonable cause for the late payment of tax, appellants must show that the failure to make a timely payment of the proper amount of tax occurred despite the exercise of ordinary business care and prudence. (*Appeal of Moren*, 2019-OTA-176P.) Taxpayers bear the burden of proving that an ordinarily intelligent and prudent businessperson would have acted similarly under the circumstances. (*Ibid.*) Asserted lack of documentation or difficulty in calculating a tax liability does not, by itself, constitute reasonable cause for a late payment of tax. (*Ibid.*) Unsupported assertions are not sufficient to satisfy the taxpayers' burden of proof. (*Appeal of GEF Operating, Inc.*, 2020-OTA-057P.)

¹ On appeal, appellants have not raised any contentions or arguments with respect to interest relief. As such, OTA finds that interest relief is not at issue and will not be discussed further.

² According to FTB, it initially construed appellants' claim for refund as a request for penalty abatement because appellants had not yet paid the liability.

Here, the late payment penalty was properly imposed because appellants failed to pay their tax liability by the due date of May 17, 2021.³ However, appellants assert that reasonable cause exists for the late payment. Appellants argue that the tax liability was a surprise. Appellants argue that they did not have the funds available on the due date and that extra time was required to liquidate investment holdings in order to make a payment. Thus, it appears that appellants are asserting a financial hardship.⁴

Financial hardship may constitute reasonable cause to excuse the late payment of tax. (*Appeal of Rougeau*, 2021-OTA-335P.) Reasonable cause based on financial hardship is explained in Treasury Regulation section 301.6651-1(c)(1), which provides that taxpayers must show the exercise of ordinary business care and prudence and that they were either unable to pay the tax or would suffer an undue hardship by paying by the due date.⁵ Treasury Regulation section 301.6651-1(c)(1) further provides that all the facts and circumstances will be considered, including the amount and nature of the taxpayer's expenditures in light of the income (or other amounts) the taxpayer could, at the time of such expenditures, reasonably expect to receive prior to the date prescribed for the payment of the tax. Thus, a taxpayer can prove ordinary business care and prudence by showing reasonable efforts to conserve sufficient assets in marketable form to satisfy the tax liability. (*Appeal of Rougeau, supra.*) However, a taxpayer who invests funds in speculative or illiquid assets has not exercised ordinary business care and prudence in providing for the payment of their tax liability unless, at the time of the investment, the remainder of the taxpayer's assets and estimated income will be sufficient to pay their tax liability. (Treas. Reg. § 301.6651(c)(1).)

Treasury Regulation section 1.6161-1(b) defines the term "undue hardship." This regulation requires that the taxpayers show that payment of the tax on the due date would have imposed "undue hardship," which requires more than merely inconveniencing the taxpayers. "It

³ See <https://www.ftb.ca.gov/about-ftb/newsroom/2020-tax-year-extension-to-file-and-pay-individual.html>.

⁴ Appellants also appear to request abatement of the penalties based on their prior good filing history. Revenue and Taxation Code section 19132.5 allows for the abatement of an individual's first-time timeliness penalties. However, as conceded by appellants, that section does not apply in the instant case (it only applies to tax years beginning on or after January 1, 2022). (R&TC, § 19132.5(a)(1), (f).)

⁵ Although there are no FTB regulations interpreting R&TC section 19132, that section is patterned after Internal Revenue Code section 6651. Therefore, the interpretation and effect given the federal provision by the federal courts and administrative bodies are relevant in determining the proper construction of the California statute. (See *Andrews v. Franchise Tax Bd.* (1969) 275 Cal.App.2d 653, 658; *Rihn v. Franchise Tax Bd.* (1955) 131 Cal.App.2d 356, 360.)

must appear that substantial financial loss, for example, loss due to the sale of property at a sacrifice price, will result to the taxpayer from making payment on the due date” (Treas. Reg. § 1.6161-1(b).)

Appellants assert that they did not have the funds available to make a timely payment of tax. However, appellants have not shown what steps, if any, were taken to conserve sufficient assets in marketable form to satisfy the liability. OTA notes that the majority of appellants’ income is wage income reported on Forms W-2. At the oral hearing, appellants asserted that the income was more than expected due to a liquidity event, but there is no evidence in support of that contention. Appellants have not provided an explanation as to why they were unable to sufficiently estimate their liability prior to the payment due date. Appellants also have not provided any evidence to support that they would suffer an undue hardship by paying by the due date. Thus, appellants have not met their burden of proof.


Last, appellants argue that the penalty is excessive and that R&TC section 21015 should be applied by analogy. However, the penalty is calculated in accordance with R&TC section 19132 and is directly correlated with the amounts that were not paid on or before the due date. As to R&TC section 21015, OTA notes that this provision of the R&TC applies to penalties imposed under R&TC sections 19011 and 19141.5. There is nothing in the law that allows OTA to extend such relief to the late payment penalty imposed in this case.

HOLDING

Appellants have not established reasonable cause for the late payment of their 2020 tax liability.


DISPOSITION

FTB's denial of appellants' claim for refund is sustained.

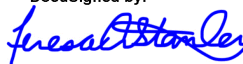
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Keith T. Long
Administrative Law Judge

We concur:

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Lauren Katagihara
Administrative Law Judge

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Teresa A. Stanley
Administrative Law Judge

Date Issued: 3/1/2024