

OFFICE OF TAX APPEALS
STATE OF CALIFORNIA

In the Matter of the Appeal of:)
GTM ARCHITECTS, INC.) OTA Case No. 230312925
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OPINION

Representing the Parties:

For Appellant: James Myers, Vice President

For Respondent: Paige Chang, Attorney

E. LAM, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19324, GTM Architects, Inc. (appellant) appeals an action by respondent Franchise Tax Board (FTB) denying appellant’s claim for refund of \$7,344, and applicable interest for the 2018 tax year; and \$7,112, and applicable interest for the 2019 tax year.¹

Appellant waived the right to an oral hearing; therefore, the Office of Tax Appeals (OTA) decides this matter based on the written record.

ISSUES

1. Whether appellant has established reasonable cause to abate the per-shareholder late filing penalties for the 2018 and 2019 tax years.
2. Whether appellant has established reasonable cause to abate the late filing penalty for the 2019 tax year.
3. Whether interest can be abated for the 2018 and 2019 tax years.

¹ Appellant’s claim for refund is comprised of the per-shareholder late filing penalties of \$7,344 for the 2018 tax year and \$6,912 for the 2019 tax year, plus a late filing penalty of \$200 for the 2019 tax year. On appeal, appellant did not request abatement of the collection cost recovery fee of \$347 for the 2018 tax year or the underpayment of estimated tax penalty of \$40.72 for the 2019 tax year. Accordingly, the collection cost recovery fee and the underpayment of estimated tax penalty are not discussed in this Opinion.

FACTUAL FINDINGS

1. Appellant is a foreign corporation based in Maryland. On June 21, 2018, appellant registered to transact business in California with the California Secretary of State (SOS).
2. Appellant elected to be taxed as an S corporation for federal and California income tax purposes.
3. On July 28, 2021, FTB sent appellant a Request for Past Due Corporation Tax Return (Request), notifying appellant that FTB had not received its California corporation tax return for the 2018 tax year, and requesting that appellant respond within 30 days.
4. In response to the Request, appellant submitted, on August 15, 2021, its California S Corporation Franchise or Income Tax Return (Form 100S) for the 2018 and 2019 tax years.
5. On appellant's 2018 Form 100S, appellant reported that the maximum number of shareholders in the S corporation at any time during the 2018 tax year was 34. The 2019 Form 100S reported a maximum of 32 shareholders in the S corporation during the 2019 tax year. Appellant also reported a zero California apportionment percentage and the \$800 minimum franchise tax due for each of the 2018 and 2019 tax years. As such, appellant remitted payment of \$800 for each tax year on August 15, 2021.
6. FTB processed appellant's Form 100S for the 2018 tax year and reduced the \$800 minimum franchise tax to zero. FTB also assessed a per-shareholder late filing penalty of \$7,344, a collection cost recovery fee of \$347, and applicable interest.
7. FTB processed appellant's Form 100S for the 2019 tax year and assessed a per-shareholder late filing penalty of \$6,912, a late filing penalty of \$200, an underpayment of estimated tax penalty of \$40.72, and applicable interest.
8. Appellant paid the balances due for the 2018 and 2019 tax years in full.² Thereafter, appellant filed FTB Form 2924, Reasonable Cause – Business Entity Claim for Refund, requesting abatement of the penalties and fees for the 2018 and 2019 tax years. FTB denied appellant's claim for refund.
9. This timely appeal followed.

² FTB canceled the remaining liability of \$23.56 for the 2019 tax year.

DISCUSSION

Issue 1: Whether appellant has established reasonable cause to abate the per-shareholder late filing penalties for the 2018 and 2019 tax years.

R&TC section 18601(a) provides that every taxpayer subject to the tax imposed by Part 11 (i.e., the Corporation Tax Law), shall file a return with FTB. While appellant alleges it was initially unaware of its filing requirement, appellant concedes on appeal that it is subject to tax and has a California filing obligation for the 2018 and 2019 tax years at issue. This is because appellant registered with the SOS as a foreign corporation qualified to transact business in California on June 21, 2018.³ (See R&TC, §§ 18601(a), 23101, 23153(b)(2), 23802.)

Pursuant to R&TC section 19172.5(a), California imposes a per-shareholder late filing penalty on an S corporation that fails to file a return on or before the due date, unless it is shown that the late filing is due to reasonable cause. The due date to file Form 100S is on or before the 15th day of the third month following the close of the S corporation's taxable year. (R&TC, § 18601(d)(1).) For the 2019 tax year, FTB postponed the due date for filing Form 100S to July 15, 2020, in response to the COVID-19 pandemic.⁴ The penalty is not measured by the tax amount due, but is instead imposed based on the number of shareholders and lateness of the return. The amount of the per-shareholder late filing penalty is calculated as \$18 multiplied by the number of persons who were shareholders in the S corporation during any part of the taxable year multiplied by the number of months (or fraction thereof) the return is late, but not to exceed 12 months. (R&TC, § 19172.5(a), (b).)

Here, appellant's 2018 tax return was due on March 15, 2019, but it was untimely filed over two years later, on August 15, 2021. The 2018 return reported a maximum of 34 shareholders during the 2018 taxable year. Therefore, FTB properly computed and imposed the 2018 per-shareholder late filing penalty of \$7,344 by multiplying \$18 by appellant's 34 shareholders and the maximum period of 12 months ($\$18 \times 34 \times 12 = \$7,344$). Appellant's

³ Appellant is not subject to the minimum franchise tax for the 2018 taxable year because 2018 was the first taxable year that appellant was qualified to do business in California. (See R&TC, § 23153(f)(1); see also R&TC, § 23802(c).) However, appellant remained subject to a tax according to or measured by its net income. (See R&TC, §§ 23151(a), 23802(b)(1), 23113.) Therefore, appellant was still required to file a return for the 2018 tax year even though it is not subject to the franchise tax for the 2018 tax year.

⁴ 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>.

2019 tax return was due on July 15, 2020, but it was untimely filed over a year later, on August 15, 2021. The 2019 return reported a maximum of 32 shareholders during the 2019 taxable year. Therefore, FTB properly computed and imposed the 2019 per-shareholder late filing penalty of \$6,912 by multiplying \$18 by appellant's 32 shareholders and the maximum period of 12 months ($\$18 \times 32 \times 12 = \$6,912$).

When FTB imposes the per-shareholder late filing penalty, the burden of proof is on the taxpayer to show that reasonable cause exists to abate the penalty. (R&TC, § 19172.5(a); see *Appeal of Quality Tax & Financial Services, Inc.*, 2018-OTA-130P.) Reasonable cause requires a showing that the taxpayer acted as an ordinary intelligent and prudent businessperson would have acted under similar circumstances. (*Appeal of Quality Tax & Financial Services, Inc.*, *supra.*)

Appellant asserts that it originally believed it did not have to file California tax returns because it did not conduct any business in California during the 2018 and 2019 tax years. Appellant contends that it promptly filed and paid its 2018 and 2019 taxes as soon as it was made aware of its filing requirements. Appellant also asserts that that none of its shareholders owed personal California income tax for either tax year. Therefore, appellant argues that the late penalty on a per-shareholder basis is excessive given the disparity between the per-shareholder late filing penalties (\$7,344 for 2018 and \$6,912 for 2019) and the \$800 minimum franchise tax that was owed by appellant for the 2019 taxable year.

Here, appellant's assertion that it was unaware of its California filing requirements because it did not conduct any business in California during the 2018 and 2019 tax years does not demonstrate that appellant acted as an ordinary intelligent and prudent businessperson. Even if appellant was unaware of a filing requirement, ignorance of the law is not an excuse for failing to file a timely return. (*Appeal of GEF Operating, Inc.*, 2020-OTA-057P.) Appellant registered with the SOS to transact business in California. Therefore, appellant should have taken steps to ascertain whether it had tax filing obligations in California as a result of its registration. On appeal, appellant does not describe any steps it took to ascertain whether it had a California tax filing obligation for 2018 or 2019.⁵ A review of the record does not show any facts and circumstances that would warrant a finding of reasonable cause. Appellant also argues that the

⁵ For example, these steps could have included consulting with a qualified tax professional for substantive advice after disclosing all relevant facts. (See *U.S. v. Boyle* (1985) 469 U.S. 241.)

per-shareholder late filing penalties are excessive. However, the computation of the penalty is provided by statute and OTA has no authority to adjust the amount or waive the penalty on the basis of alleged excessiveness. (See, e.g., *Appeal of Daneshgar*, 2021-OTA-210P, *Appeal of Porreca*, 2018-OTA-095P.) Accordingly, appellant has not established reasonable cause to abate the per-shareholder late filing penalty for the 2018 and 2019 tax years.

Issue 2: Whether appellant has established reasonable cause to abate the late filing penalty for the 2019 tax year.

Under R&TC section 19131, California imposes a late filing penalty for the failure to file a return by its due date, unless the failure to file was due to reasonable cause and not due to willful neglect. The late filing penalty imposed by R&TC section 19131 is a separate and distinct penalty from the per-shareholder late filing penalty imposed by R&TC section 19172.5(a) which is discussed above. The amount of the late filing penalty is 5 percent of the amount of tax required to be shown on the return for every month that the return is late, without regard to extensions of time for filing, up to a maximum of 25 percent. (R&TC, § 19131(a).) As relevant to this appeal, appellant filed its 2019 Form 100S on August 15, 2021, over a year after the July 15, 2020 postponed due date. Therefore, FTB properly imposed the maximum late filing penalty of \$200 for the 2019 tax year (the \$800 tax due times 25 percent).⁶

As with the per-shareholder late filing penalty, the taxpayer bears the burden of proving reasonable cause exists, which requires a showing that it acted as an ordinary intelligent and prudent businessperson would have acted under similar circumstances. (*Appeal of GEF Operating, Inc., supra.*)

Here, appellant presents the same argument as it did for the per-shareholder late filing penalties. However, for the reasons expressed above, appellant also has not established reasonable cause to abate the late filing penalty for the 2019 tax year.

Issue 3: Whether interest can be abated for the 2018 and 2019 tax years.

If any amount of tax is not paid by the due date, interest is required to be imposed from the due date until the date the taxes are paid. (R&TC, § 19101(a).) Interest also accrues on any unpaid penalty amount if the penalty is not paid within 15 calendar days from the date of notice

⁶ FTB did not impose a late filing penalty for the 2018 tax year because no tax was due on the late filed return.

and demand, and in that case, interest shall be imposed for the period from the date of the notice and demand to the date of payment. (R&TC, § 19101(c)(2)(A).) Interest is not a penalty but is compensation for the taxpayer's use of money that should have been paid to the state. (*Appeal of Balch*, 2018-OTA-159P.) Imposition of interest is mandatory, and it can only be abated in certain limited situations when authorized by law. (R&TC, § 19101(a); *Appeal of Balch, supra*.)

There is no reasonable cause exception to the imposition of interest. (*Appeal of Moy*, 2019-OTA-057P.) Rather, to obtain relief from interest, appellant must qualify under R&TC sections 19104 or 21012.⁷ Under R&TC section 19104, FTB is authorized to abate interest if there has been an unreasonable error or delay in the performance of a ministerial or managerial act by an employee of FTB. Appellant does not assert, nor does the record show, that FTB committed such errors or delays. R&TC section 21012 is also not relevant here because evidence in the record does not demonstrate that FTB provided appellant with any written advice. Accordingly, appellant is not entitled to interest abatement for the 2018 and 2019 tax years.

⁷ FTB may grant a waiver of interest when it “determines that an individual or fiduciary demonstrates inability to pay that interest solely because of extreme financial hardship caused by significant disability or other catastrophic circumstance.” (R&TC, § 19112.) However, appellant is a S Corporation, not an individual or fiduciary, making R&TC section 19112 inapplicable to appellant. Furthermore, OTA has no jurisdiction to determine whether a taxpayer is entitled to the abatement of interest under R&TC section 19112. (*Appeal of Moy, supra*.)

HOLDINGS

1. Appellant has not established reasonable cause to abate the per-shareholder late filing penalties for the 2018 and 2019 tax years.
2. Appellant has not established reasonable cause to abate the late filing penalty for the 2019 tax year.
3. Interest cannot be abated for the 2018 and 2019 tax years.

DISPOSITION

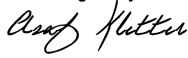
FTB’s action in denying appellant’s claim for refund is sustained.

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 Eddy Y.H. Lam
 Administrative Law Judge

We concur:

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 Cheryl L. Akin
 Administrative Law Judge

Date Issued: 3/5/2024