

FACTUAL FINDINGS

1. Appellants made the following estimated tax payments for the 2021 tax year: on May 17, 2021, a first quarter payment of \$12,093; on June 9, 2021, a second quarter payment of \$20,000; on September 15, 2021, a third quarter payment of \$20,000, on January 15, 2022, a fourth quarter payment of \$7,000; and on July 11, 2022, a payment of \$279,000. Appellants' estimated payments totaled \$338,093.
2. Appellants timely filed a joint 2021 California Nonresident or Part-Year Resident Income Tax Return (return) reporting total tax of \$336,602, total payments of \$338,104,² and overpaid tax of \$1,502. Appellants self-assessed an estimated tax penalty of \$2,995, elected to apply the overpaid tax against the liability, and calculated a remaining amount due of \$1,493 (\$2,995 - \$1,502), which they paid on October 15, 2022.
3. On November 21, 2022, FTB issued appellants a Notice of Tax Return Change – Revised Balance (notice), which imposed a late payment penalty of \$18,037.37, and reduced appellants' estimated tax penalty to \$2,994. The notice also assessed applicable interest.
4. Appellants paid the remaining amount due and filed a timely claim for refund to abate the late payment penalty, the estimated tax penalty and associated interest.
5. On April 10, 2023, FTB sent appellants a Claim for Refund Denied letter, and on the same day, separately issued appellants a letter denying the estimated tax penalty refund.
6. This timely appeal followed.

DISCUSSION

Issue 1: Whether appellants have shown reasonable cause to abate the late payment penalty.

R&TC section 19132(a)(1)(A) imposes a late payment penalty when a taxpayer fails to pay the amount shown as tax on the return by the date prescribed for the payment of the 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.) For individual filers, the 2021 return was due on April 15, 2022. (See R&TC, § 18566.) When FTB imposes a penalty, the law presumes that the penalty was imposed correctly, and the taxpayer bears the burden of proof to establish otherwise. (*Appeal of Xie*, 2018-OTA-076P.)

² Appellants also reported California income tax withholding of \$11 (\$338,093 + \$11 = \$338,104).

Here, FTB imposed the late payment penalty because April 15, 2022, was the payment due date for the 2021 tax year, but appellants did not fully satisfy their 2021 tax liability until October 15, 2022, six months later. Appellants do not dispute FTB's calculations; rather, appellants assert reasonable cause to abate the late payment penalty.

The late payment penalty may be abated where the taxpayer shows 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).) To establish reasonable cause for the late payment of tax, a taxpayer must show that 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 (*Moren*)). The taxpayer bears 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 the late payment of tax. (*Ibid.*) The most important factor in determining reasonable cause and good faith is the extent of the taxpayer's effort to assess his or her proper tax liability. (*Ibid.*) Unsupported assertions are insufficient to satisfy a taxpayer's burden of proof. (*Ibid.*) To overcome the presumption of correctness attached to the penalty, a taxpayer must provide credible and competent evidence supporting a claim of reasonable cause, otherwise, the penalty cannot be abated. (*Appeal of Xie, supra.*)

Illness may establish reasonable cause where the taxpayer presents credible and competent proof that the circumstances of the illness prevented the taxpayer from complying with the law. (*Appeal of Triple Crown Baseball LLC*, 2019-OTA-025P; see also *Appeal of Head and Feliciano*; 2020-OTA-127P.) However, if the difficulties simply caused the taxpayers to sacrifice the timeliness of one aspect of their affairs to pursue other aspects, the taxpayers must bear the consequences of that choice. (*Appeal of Triple Crown Baseball LLC, supra.*) An acceptable reason for failure to pay taxes will excuse such failure only as long as the reason remains valid. (*Ibid.*)

Here, appellants claim they had reasonable cause as follows: during the 2021 tax year, appellants sold their business, a limited liability company (LLC); the tax treatment and income allocations of the entity were very complicated, and the complex structure required an intense and thorough analysis; and the financial information needed to accurately calculate (and pay)

appellants' tax liability was unknown at the time of filing.³ Second, appellants assert that in 2021 and 2022, appellant A. Maleh was dealing with a medical emergency which required him to be in the hospital for treatment and which prevented him from timely paying the tax due.

Concerning appellants' claim that the LLC's tax treatment and income allocations were very complicated and required thorough analysis, difficulty in calculating a tax liability does not, by itself, constitute reasonable cause for the late payment of tax. (*Moren, supra.*) Moreover, appellants have not explained with credible evidence what financial information was unknown, who possessed the relevant records, and what efforts appellants made to obtain the records and assess their tax liability. (*Ibid.*) Appellants have not provided substantiation to support their claims, and accordingly, the penalty cannot be abated on this ground. (*Appeal of Xie, supra.*)

Regarding appellants' claim that in 2021 and 2022, appellant A. Maleh was dealing with a medical emergency which prevented him from timely paying appellants' tax liability, illness may establish reasonable cause for the period in which it prevented the taxpayers from complying with the law. (*Appeal of Moren, supra.*) However, appellants have not provided documentation substantiating appellant A. Maleh's illness or the period(s) during which appellant A. Maleh was completely prevented from paying appellants' tax liability. Furthermore, appellants provide no evidence to show that appellant S. Maleh was unable to make the payment in lieu of appellant A. Maleh, who appellants allege was unable to make the payment. (See *Appeal of Head and Feliciano, supra.*) Appellants have not supported their claim of reasonable cause based on appellant A. Maleh's medical emergency, and the late payment penalty may not be abated on this ground. (*Appeal of Xie, supra.*)

Issue 2: Whether the estimated tax penalty may be waived or abated.

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

³ On appeal, FTB provides evidence to contradict appellants' assertions. FTB proffers the first pages of the LLC's 2008 through 2021 Schedules K-1 issued to appellant A. Maleh to show that he had a continued interest in the LLC. FTB also submits the LLC's 2021 tax return, which shows that the LLC had only two members during the 2021 tax year. However, as appellants have not substantiated their claims, there is no need to address FTB's proffered evidence.

penalty, where taxpayers fail to timely pay estimated tax.⁴ 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 2021 tax year, appellants' adjusted gross income (AGI) exceeded \$1 million and therefore the required annual payment was 90 percent of the tax shown on the return. (R&TC, § 19136.3; IRC, § 6654(d)(1)(B)(i).) Appellants' 2021 tax liability was \$336,602, and the required annual payment was thus \$302,941.80. Appellants underpaid each of the required estimated tax payments, and therefore, FTB properly imposed the estimated tax penalty.⁵

Appellants do not contest the imposition or computation of the estimated tax penalty. Rather, appellants present arguments for waiver of the estimated tax penalty for reasonable cause. However, there is no provision in the IRC or R&TC that allows the estimated tax penalty to be abated solely on a finding of reasonable cause. (*Appeal of Saltzman*, 2019-OTA-070P.) As a result, there is no general reasonable cause exception to the imposition of the estimated tax penalty; the penalty is mandatory unless the taxpayer establishes 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."⁶

⁴ 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. (See also IRC, § 6654(c)(2) [specifying required installment due dates].) For federal income tax purposes, an additional installment is also due by September 15 of the applicable tax year.

⁵ The first quarter estimated tax payment installment is generally 30 percent of the required annual payment, here, \$90,882.54 ($\$302,941.80 \times 0.30 = \$90,882.54$). (R&TC, § 19136.1(a)(2)(A).) Appellants' May 17, 2021 payment of \$12,093 was untimely. Thus, appellants underpaid the first quarter installment.

The second quarter estimated tax payment installment is generally 40 percent of the required annual payment, here, \$121,176.72 ($\$302,941.80 \times 0.40 = \$121,176.72$). (R&TC, § 19136.1(a)(2)(B).) Appellants made a timely payment of \$20,000. Thus, appellants underpaid the second quarter installment.

The fourth quarter estimated tax payment installment is generally 30 percent of the required annual payment, here, \$90,882.54 ($\$302,941.80 \times 0.30 = \$90,882.54$). (R&TC, § 19136.1(a)(2)(D).) Appellants made a timely payment of \$7,000. Thus, appellants underpaid the fourth quarter installment.

⁶ IRC section 6654(e)(3)(B) provides that FTB may waive the tax 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. Appellants have not alleged that this exception applies, this Opinion will not discuss it further.

The exception for unusual circumstances is considerably narrower than reasonable cause. (*Appeal of Mazdyasni*, 2018-OTA-049P.) The phrase “casualty, disaster, or other unusual circumstances” generally refers to unexpected events that cause a hardship or loss such that, due to the circumstances, it would be “against equity and good conscience” to impose the estimated tax penalty. (*Appeal of Saltzman, supra.*)

Several cases have considered whether unusual circumstances warranted waiver under IRC section 6654(e)(3)(A). In *Farhoumand v. Commissioner*, T.C. Memo. 2012-131, the tax court determined that stock market volatility resulting in a higher tax liability was not an unusual circumstance justifying waiver of the estimated tax penalty. In *Appeal of Johnson, supra*, OTA held that unexpectedly high income from the profitable sale of real property was not an unusual circumstance justifying waiver of the estimated tax penalty. In *Appeal of Mazdyasni, supra*, OTA held that difficulty in estimating partnership income from the profitable sale of a taxpayer’s partnership interest is not an unusual circumstance justifying waiver. Finally, in *Appeal of Saltzman, supra*, OTA held that a partner’s unexpected receipt of a guaranteed payment from a partnership is not an unusual circumstance justifying waiver.

Appellants do not specifically address the estimated tax penalty. Thus, OTA interprets appellants to assert the same reasonable cause grounds as described under the late payment penalty. However, a partner’s distributive share of income, which is reported on a Schedule K-1, is not excludable from the estimated tax requirements merely because such income is not known until a Schedule K-1 is received at the close of a tax year. (*Appeal of Mazdyasni, supra.*) Here, appellants have not established why they were unable to obtain the necessary financial information to estimate the amount of their 2021 income. (*Appeal of Mazdyasni, supra.*)

Moreover, the authorities set forth above indicate that unexpectedly high income or a higher tax liability than normal is not an unusual circumstance warranting waiver of the estimated tax penalty. (*Ibid; Appeal of Saltzman, supra, Appeal of Johnson, supra.*) Rather than suffering an unexpected hardship or loss, appellants received substantial income. (*Appeal of*

Saltzman, supra.) Thus, imposing an interest charge on the tax due on the income appellant received does not offend “equity and good conscience.” (*Ibid.*)⁷

Issue 3: Whether appellants are entitled to interest abatement.

Interest must be assessed from the date a tax payment is due through the date that it is paid. (R&TC, § 19101(a).) Imposing interest is mandatory; it is not a penalty, but it is compensation for the taxpayers’ 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 R&TC section 19104 or 21012.⁸ Pursuant to 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. Pursuant to R&TC section 21012, taxpayers may be relieved of interest where they reasonably relied on written advice from FTB.

Appellants do not allege that either statutory provision for interest abatement applies to the facts of this case, and OTA concludes based on the evidence in the record that no statutory provision for abatement applies. Therefore, there is no basis to abate interest.

⁷ Appellants also request that OTA present their request for penalty abatement to the Franchise Tax Board’s Chief Counsel. OTA’s authority to act is of limited jurisdiction and it “has no powers except such as the law of its creation has given it.” (*Appeal of Moy*, 2019-OTA-057P; *Ferdig v. State Personnel Board* (1969) 71 Cal.2d 96, 105.) OTA’s function in this appeal is to determine the correct amount of a taxpayer’s California income tax liability. No statute or provision authorizes OTA, on appellants’ behalf, to request penalty abatement from the Franchise Tax Board’s Chief Counsel.

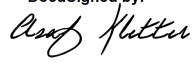
⁸ Under R&TC section 19112, FTB may waive interest for any period for which it determines that an individual or fiduciary is unable to pay interest due to extreme financial hardship. OTA does not have authority to review FTB’s denial of a request to waive interest under R&TC section 19112. (*Appeal of Moy, supra.*)

HOLDINGS

1. Appellants have not shown reasonable cause to abate the late payment penalty.
2. The estimated tax penalty may not be waived or abated.
3. Appellants are not entitled to interest abatement.


DISPOSITION

FTB’s actions denying appellants’ claims for refund are sustained.


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 Asaf Kletter
 Administrative Law Judge

We concur:

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 Josh Lambert
 Administrative Law Judge

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 Administrative Law Judge

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