

In the Matter of the Appeal of:) OTA Case No. 240917559
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1. Whether appellant has shown error in respondent's proposed assessment of additional tax.
2. Whether the late filing penalty should be waived.
3. Whether the demand penalty should be waived.
4. Whether the filing enforcement fee should be waived.
5. Whether there are grounds for the abatement of interest.

FACTUAL FINDINGS

1. As part of its Integrated Non-Filer Compliance (INC) program, respondent obtained information that appellant filed a federal income tax return with the IRS for the 2021 tax year using a California address.
2. Respondent issued appellant a Demand for Tax Return notice dated February 6, 2024, requiring appellant submit a copy return if previously filed, file a return, or provide information showing that he had no filing requirement.
3. After not receiving a response, respondent issued a Notice of Proposed Assessment (NPA) for the 2021 tax year on April 19, 2024. The NPA reflected estimated income produced from a series of federal form 1099s of \$198,346, and proposed a tax liability of \$14,873, a late filing penalty of \$3,718.25, a demand penalty of \$3,718.25, and a filing enforcement fee of \$108, plus accrued interest.
4. On June 14, 2024, appellant filed a protest with respondent, disagreeing with the NPA.
5. Respondent issued a Notice of Action on August 22, 2024, affirming the NPA.
6. This timely appeal followed.
7. On appeal, appellant submitted additional briefing requesting relief from the penalties and interest. As of the date briefing closed, appellant has not filed a California income tax return.

DISCUSSION

Issue 1: Whether appellant has shown error in respondent's proposed assessment of additional tax.

California residents are taxed on their entire taxable income regardless of the source of that income. (R&TC, § 17041(a).) Every individual subject to the Personal Income Tax Law is required to make and file a return with respondent "stating specifically the items of the individual's gross income from all sources and the deduction and credits allowable," in excess of certain filing thresholds. (R&TC, § 18501(a).) For the 2021 taxable year, single individuals under the age of 65 with no dependents and gross income of at least \$19,310 or adjusted gross income of at least \$15,448, are required to file a Form 540. (R&TC, § 18501(a), (d).) In relevant part, R&TC section 19087(a) provides that if any taxpayer fails to file a return for any taxable year, respondent, at any time, may require a return under penalties of perjury or may make an estimate of the taxpayer's net income, from any available information, and may propose to assess the amount of tax, interest, and penalties due.

When respondent makes a proposed assessment of tax based on an estimate of income, respondent's initial burden is to show why its proposed assessment is reasonable and rational. (See *Todd v. McColgan* (1949) 89 Cal.App.2d 509.) An assessment based on unreported income is presumed correct when the taxing agency introduces a minimal factual foundation to support the assessment. (*In re Olshan* (9th Cir.2004) 356 F.3d 1078, 1084.) Once respondent has met its initial burden, the proposed assessment of tax is presumed correct, and the taxpayer has the burden of proving it to be wrong. (*Todd v. McColgan, supra.*) Unsupported assertions are insufficient to satisfy a taxpayer's burden of proof. (*Appeal of Scanlon*, 2018-OTA-075P.) In the absence of credible, competent, and relevant evidence showing error in respondent's determination, the determination must be upheld. (*Appeal of Davis and Hunter-Davis*, 2020-OTA-182P.)

The R&TC defines "gross income" and "adjusted gross income" by referring to and incorporating into California law Internal Revenue Code (IRC) sections 61 and 62, respectively. (R&TC, §§ 17071, 17072.) Unless otherwise provided, "gross income means all income from whatever source derived," including compensation for services, interest, dividends, and pensions. (IRC, § 61(a).) Income generally includes any "accessions to wealth." (*Commissioner v. Glenshaw Glass Co.* (1955) 348 U.S. 426, 431.)

Here, appellant does not contest the method used by respondent to estimate their income or the amount of income estimated therefrom. Respondent's estimate of appellant's gross income was derived from adjusted gross income reported on appellant's federal income tax return. That estimate was supported by a series of federal Form 1099s received by respondent which appear to corroborate appellant's assertion that their income was not earned via wages, but capital gains. However, in contrast to federal capital gains tax rates, which depend on the length of time a taxpayer holds a capital asset, California does not provide a different tax rate for capital gains; capital gains are taxed as ordinary income. Because the gross income attributed to appellant exceeded the filing threshold for 2021, respondent correctly determined that appellant had a California filing requirement for that taxable year. Because respondent established a minimal factual foundation for its determination, the NPA is presumed correct, and the burden of proof shifts to appellant to show error in respondent's determination.

Appellant initially challenges respondent's determination that additional tax was owing claiming to have already paid any taxes due for the year. However, appellant fails to further explain the error in the proposed assessment. In subsequent briefing, appellant limits the scope of their appeal to relief from penalties, interest, and the enforcement fee. Because respondent

substantiated the basis for the proposed assessment and appellant failed to show the proposed assessment was wrong, respondent's assessment of tax is sustained.

Issue 2: Whether the late filing penalty should be waived.

Individual taxpayers filing on a calendar year basis are required to file their Forms 540 on or before April 15th following the close of the calendar year. (R&TC, § 18566.) A late filing penalty is imposed when a taxpayer fails to file a tax return by either the due date or the extended due date, unless the taxpayer establishes that the late filing was due to reasonable cause and not due to willful neglect. (R&TC, § 19131(a).) When respondent imposes a penalty, the law presumes that the penalty was imposed correctly. (*Appeal of Xie*, 2018-OTA-076P.)

The taxpayer bears the burden of proving that reasonable cause exists to support a waiver of the penalty. (*Appeal of Wright Capital Holdings LLC*, 2019-OTA-219P; *Appeal of Triple Crown Baseball LLC*, 2019-OTA-025P.) To establish reasonable cause, the taxpayer must show that the failure to file timely returns occurred despite the exercise of ordinary business care and prudence, or that such cause existed as would prompt an ordinarily intelligent and prudent businessperson to have so acted under similar circumstances. (*Appeal of Head and Feliciano*, 2020-OTA-127P.) Unsupported assertions are insufficient to satisfy a taxpayer's burden of proof. (*Appeal of Wright Capital Holdings LLC*, *supra*.)

Appellant first requests one-time penalty abatement under R&TC § 19132.5(b). However, California's one time abatement program is only effective for tax years beginning on or after January 1, 2022. (See R&TC, § 19132.5(a), (f).) Appellant's appeal is for the 2021 tax year; therefore, one-time abatement is not available.

Appellant presents a detailed argument for relief for reasonable cause based on their location out-of-state during 2024 and 2025 in pursuit of higher education. Appellant asserts that the rigors of that endeavor, coupled with their being away from California, substantially impaired appellant's access to financial records to complete their return or be made aware of the notices sent by respondent, which consequently went unanswered. Appellant notes their history of good compliance and that they took prompt remedial steps to ensure future compliance with California tax obligations. Finally, appellant notes the significant financial hardship from the assessment of the additional penalties.

Generally, the most important factor in determining whether the taxpayer has reasonable cause and acted in good faith is the extent of the taxpayer's effort to report the proper tax liability. (*Appeal of Moren*, 2019-OTA-176P; *Frias v. Commissioner* (2017) T.C. Memo. 2017-139, *16-17.) While appellant's circumstances may well have been of a kind that created

difficulties for them, appellant fails to address the central question, which is why those circumstances impeded their ability to file in *April of 2022*, when the return was due. Appellant also fails to explain why they have not filed a return since appellant became aware of the respondent's proposed assessment. If the difficulties faced by a taxpayer simply cause them to sacrifice the timeliness of one aspect of their affairs to pursue other aspects, the taxpayer must bear the consequences of that choice. (*Appeal of Head and Feliciano, supra.*) The taxpayer's selective inability to perform tax obligations, while participating in regular business activities, does not establish reasonable cause. (*Ibid.*) Therefore, appellant has not established reasonable cause to abate the late filing penalty.

Issue 3: Whether the demand penalty should be waived.

California imposes a demand penalty for failing to file a return or provide information upon respondent's notice and demand to do so, unless the failure to do so was due to reasonable cause and not willful neglect. (R&TC, § 19133.) The burden is on the taxpayer to prove that reasonable cause existed. (*Appeal of GEF Operating, Inc.*, 2020-OTA-057P; *Appeal of James* (83-SBE-009) 1983 WL 15396.) The framework for determining the existence of reasonable cause under the demand penalty is virtually identical to that under the late filing penalty outlined above. (See *Appeal of Belcher*, 2021-OTA-284P; *Appeal of GEF Operating, Inc., supra.*)

Respondent will only impose a demand penalty if the taxpayer fails to respond to a current Demand for Tax Return in the manner prescribed and respondent issued an NPA under the authority of R&TC section 19087(a) after the taxpayer failed to timely respond to a Request for Tax Return or a Demand for Tax Return at any time during the four-taxable-year period immediately preceding the tax year for which the current Demand for Tax Return is issued. (Cal. Code Regs., tit. 18, § 19133(b).)

Here, respondent issued the Demand to appellant in February 2024, and the Demand afforded appellant sufficient opportunity to comply. As of the date briefing closed, appellant has failed to file a return for the 2021 tax year. Moreover, respondent issued an NPA for the 2019 tax year after appellant failed to timely respond to a Request for Tax Return. Hence, respondent has satisfied the legal requirements for imposing the demand penalty, and appellant must now establish reasonable cause for relief from the demand penalty.

Here, appellant's central argument of being out of state in pursuit of higher education is proximate to the pre-conditions for imposition of the penalty. However, in absence of providing

notice to respondent of a relocation, respondent's reliance on appellant's last known address was valid. (R&TC, § 18416(b).)¹

Here as well, appellant has simply sacrificed the timeliness of one aspect of their affairs to pursue other aspects and must bear the consequences of that choice. (*Appeal of Head and Feliciano, supra.*) The selective inability to fulfil their tax obligations, while participating in regular business activities, does not establish reasonable cause. (*Ibid.*) Therefore, the demand penalty cannot be abated.

Issue 4: Whether the filing enforcement fee should be waived.

A filing enforcement fee shall be imposed if a taxpayer fails or refuses to make and file a required tax return within 25 days after respondent mails a formal legal demand to file the tax return. (R&TC, § 19254(a)(2).) Once the fee is properly imposed, the statute provides no grounds, including reasonable cause, upon which the fee may be abated. (R&TC, § 19254; see *Appeal of Shanahan*, 2024-OTA-039P.) Therefore, the inquiry is limited to whether respondent complied with the statutory notice requirements for imposing the filing enforcement fee.

Here, respondent issued appellant a Demand for the 2021 taxable year, notifying them that it would impose a filing enforcement fee if they had a filing requirement and failed to file a 2021 Form 540 by the due date stated in the Demand. Respondent properly imposed the fee after appellant, who had a 2021 filing requirement, did not file a tax return. While appellant notes having temporarily relocated out of state for their graduate studies and subsequently resolving the prior address issue with respondent, there is no assertion by appellant that the last known address relied upon by respondent was inaccurate or invalid at the time of mailing. Appellant only argues the temporary relocation substantially impaired their notification. Since the fee was properly imposed, there is no authority for the waiver of this fee.

Issue 5: Whether there are grounds for the abatement of interest.

Tax is due on the original due date of the return without regard to any filing extension. (R&TC, § 19001.) If a taxpayer does not pay the tax by the original due date of the tax return, or if respondent assesses additional tax, the law provides for charging interest at the adjusted annual rate established on the balance due. (R&TC, § 19101.) Imposing interest is mandatory, and respondent cannot abate interest except where authorized by law. (*Appeal of Balch*,

¹ The last known address is the address that appears on the taxpayer's last return filed with respondent, unless the taxpayer has provided to respondent clear and concise written or electronic notification of a different address or respondent has an address it has reason to believe is the most current address for the taxpayer. (R&TC, § 18416(c).)

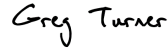
2018-OTA-159P.) Interest is not a penalty; it is compensation for the use of money. (*Ibid.*) To obtain waiver or abatement of interest, appellant must qualify under R&TC section 19104, 19112, or 21012. (*Ibid.*) Appellant has not alleged, and no evidence in the record indicates that any of these statutory provisions apply. Therefore, appellant did not establish that they qualified for any waiver or abatement of interest.

HOLDINGS²

1. Appellant has failed to show error in respondent's assessment of additional tax.
2. The late filing penalty should not be waived.
3. The demand penalty should not be waived.
4. The filing enforcement fee should not be waived.
5. There are no grounds for the abatement of interest.

DISPOSITION

Respondent's action is sustained.

Signed by:

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Greg Turner
Administrative Law Judge

We concur:

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Amanda Vassigh
Administrative Law Judge

Signed by:

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Suzanne B. Brown
Administrative Law Judge

Date Issued: 7/21/2026

² Respondent may consider appellant's inability to pay under its payment arrangement or offer-in-compromise programs. If appellant is experiencing difficulties in paying their liabilities once the decision in this appeal is final, they may contact respondent to discuss payment options. (See <https://www.ftb.ca.gov/pay/if-you-cant-pay/index.html>.)