

1 Josh Lambert
2 Tax Counsel
3 Board of Equalization, Appeals Division
4 450 N Street, MIC: 85
5 PO Box 942879
6 Sacramento, CA 95814
7 Tel: (916) 322-3284
8 Fax: (916) 324-2618

6 Attorney for the Appeals Division

7 **BOARD OF EQUALIZATION**

8 **STATE OF CALIFORNIA**

9
10 In the Matter of the Appeal of:) **HEARING SUMMARY**
11) **PERSONAL INCOME TAX APPEAL**
12 **MICHAEL I. COHEN**) Case No. 795873

13
14

	<u>Year</u>	<u>Refund</u>
	2010	Claim ¹
		\$2,710.25

15
16 Representing the Parties:

17 For Appellant: Taxpayer Appeals Assistance Program (TAAP)²
18 For Franchise Tax Board: David Muradyan, Tax Counsel

19
20 QUESTION: Whether appellant has shown that he had reasonable cause for failing to reply to
21 respondent's Demand for Tax Return (Demand).

22
23 HEARING SUMMARY

24 Background

25 The Franchise Tax Board's (respondent or FTB) Integrated Non-Filer Compliance (INC)

26
27 ¹ This is the amount of the demand penalty.

28 ² Appellant filed the appeal letter. Wilton Robinson of TAAP filed the reply brief and supplemental brief.

1 Program annually matches income records obtained from various reporting sources against filed tax
2 returns to identify individuals who may not have fulfilled their legal requirement to file a California
3 income tax return. As part of the program, respondent obtains information from financial institutions
4 showing interest income and dividend income, among other types of income. For the 2010 tax year,
5 respondent obtained an Internal Revenue Service (IRS) Form 1099-INT or 1099-OID showing that
6 appellant received interest income, an IRS Form 1099-DIV showing that appellant received dividend
7 income, and an IRS Form 1099-B showing that appellant received proceeds from a broker exchange,
8 among others. Based on this information, respondent determined that appellant had received income
9 sufficient to prompt a return-filing requirement.³ (Resp. Op. Br., p. 1; Ex. A.)

10 Because appellant had not timely filed a 2010 return, respondent sent appellant a
11 Demand on February 1, 2012, requiring appellant to either file a 2010 return or explain why a 2010
12 return was not required. The Demand required a reply by March 7, 2012. On April 2, 2012, after
13 appellant failed to respond to the Demand, respondent issued a Notice of Proposed Assessment (NPA)
14 for the 2010 tax year, based on appellant's estimated income of \$658,076.51.⁴ The NPA proposed an
15 assessment of tax of \$40,206.00, a late filing penalty of \$10,051.50, a demand penalty of \$15,051.50,
16 and a filing enforcement fee of \$88.00, plus interest. (Resp. Op. Br., pp. 1-2; Exs. A & B.)

17 On April 15, 2012, appellant filed his 2010 California income tax return.⁵ Appellant
18 reported a federal adjusted gross income (AGI) of \$143,367. After adjustments, deductions and
19 application of the exemption credit, appellant reported a self-assessed tax of \$10,841. After also
20 accounting for an estimated tax payment of \$20,000 and a self-assessed use tax of \$68, appellant
21 claimed an overpayment of \$9,091 (i.e., \$9,159 less \$68 use tax), plus a \$23 self-assessed penalty for
22 underpayment of estimated tax. (Resp. Op. Br., p. 2; Exs. C & G.)

23 _____
24 ³ For the 2010 tax year, a single individual with no dependents realizing gross income of \$14,754 or adjusted gross income
25 of \$11,803 was required to file a California income tax return.

26 ⁴ The total estimated income of \$658,076.51 was broken down as follows: \$4,739.00 in interest income, \$16,895.00 in
27 dividend income, \$208,729.00 in miscellaneous income, and \$427,713.51 that appellant received from proceeds from a
broker exchange. (Resp. Op. Br., p. 2; Ex. B.)

28 ⁵ Appellant also filed his 2010 federal tax return approximately one year late, on April 17, 2012. (Resp. Op. Br., p. 2;
federal Account Transcript, Ex. D.)

1 Respondent accepted and processed appellant's return and adjusted appellant's total tax
2 down to \$10,841, the self-assessed amount. Because the tax was reduced following respondent's
3 processing of appellant's return, so too was the demand penalty (reduced to \$2,710.25.) Appellant also
4 removed the late filing penalty. Respondent applied the resulting overpayment to cover a tax liability
5 from the 2011 tax year in the amount of \$4,552.94, the self-assessed use tax of \$68.00, the
6 underpayment of estimated taxes penalty of \$179.74, and the reduced demand penalty in the amount of
7 \$2,710.25, leaving a refund amount of \$1,678.40, which was refunded to appellant on June 5, 2012.
8 (Resp. Op. Br., p. 2; Exs. C & E.)

9 Appellant filed a claim for refund, arguing that the penalties should be dismissed because
10 he delayed filing his tax return due to the death of his mother on December 27, 2010. As a result of his
11 mother's passing, appellant stated he had to deal with her estate, her estate taxes, and her 2010 personal
12 taxes. On November 14, 2013, respondent denied appellant's claim for refund of the demand penalty on
13 the grounds that appellant had not shown reasonable cause for failing to file after notice and demand.
14 This timely appeal followed. (Resp. Op. Br., pp. 2-3; Appeal Letter, attachments.)

15 Contentions

16 Appeal Letter

17 Appellant asserts that there is reasonable cause for the delay in filing his 2010 tax return
18 due to his mother's illness and death from breast cancer in 2010 while out of state in Las Vegas, NV.
19 Appellant states that the situation required life-and-death emergency actions by him that caused him to
20 be with her during much of 2010, thereby physically separating him from his business and records in
21 California. Appellant states that continuing into 2011, he was required to be in Las Vegas arranging and
22 attending her funeral, and locating and sorting through her records to deal with her estate and tax
23 matters, which he expected to involve inheritance that would affect his federal and California tax
24 liabilities in 2010 and/or 2011. (Appeal Letter, p. 1.)

25 Appellant argues that the extraordinary once-in-a-lifetime circumstances of his mother's
26 illness and death, and his dealing with her personal and inheritance/estate tax affairs were reasonable
27 cause for him to file his federal and State 2010 and 2011 tax returns all at once in April 2012.
28 Appellant states that he knows and believes that any ordinary person faced with these same

1 circumstances would have acted similarly. Appellant states that he is a single, self-employed,
2 individual taxpayer who always takes his tax obligations seriously and typically overpays his taxes each
3 year and then files for a refund. Appellant states that since his annual taxes are intentionally overpaid,
4 as they were in 2010, he has every financial incentive to file tax returns as soon as possible. (Appeal
5 Letter, p. 1.)

6 Appellant states that, during June 2010, he was summoned by an emergency call from his
7 sister, herself a senior, to go to their mother's house in Las Vegas, where he found their mother in bad
8 condition. Appellant states that he and his sister were responsible for months thereafter to recover their
9 mother, to clean/sterilize the house, to communicate with her doctors, to enter her into a nursing facility
10 where they rebalanced her medications, to return her to her home, to initiate hospice care, to interview,
11 hire, and supervise a series of private home caregivers, and to be her end-of-life caregivers from
12 June 2010 until her death on December 27, 2010. Appellant states that the circumstances of his
13 mother's death at the end of the 2010 tax period also created many issues and questions as to the effect
14 of her death, her financial affairs, her estate and taxes, and inheritance on his personal tax affairs for
15 2010 and/or 2011, in addition to the effects of physically separating him from his normal business and
16 records described during much of the second half of 2010 and well into 2011. (Appeal Letter, p. 2.)

17 Appellant states that, all he could reasonably do at the end of 2010, was to pay estimated
18 taxes for 2010, allowing for a potential inheritance tax for 2010, which he did in excess, sending
19 \$20,000 to the FTB towards his ultimate liability of about \$10,000, which he mailed from Las Vegas.
20 Appellant states that, in early 2011, while grieving this loss, and sorting through mother's tax and
21 financial affairs, which he believed would have a direct effect on his tax affairs for 2010 and/or 2011, all
22 he could reasonably do, was to complete her final 2010 personal tax return. Appellant states that his
23 sister signed as their mother's executor, and they filed from Las Vegas in April 2011. (Appeal Letter, p.
24 2.)

25 Appellant states that during 2011 and into 2012, he made a good faith, responsible, and
26 diligent effort to understand, address, and complete his personal tax matters for 2010 and 2011 and to
27 properly account for the effects of his mother's estate taxes and his resulting inheritance. Appellant
28 states that, although he has always believed that an ordinary taxpayer should not be required to hire an

1 accountant nor an attorney in order to pay one's taxes, unfortunately, he was not able to figure out how
2 to complete his mother's estate tax return and his inheritance taxes on his own, even with the help of the
3 most advanced tax software available to consumers. (Appeal Letter, p. 2.)

4 Appellant states that, frustrated by the complexity and difficulty of his mother's estate
5 tax return and his resulting inheritance tax liability related to her death in 2010, ultimately on
6 March 21, 2012, he hired a professional accountant to help. Appellant states that with the accountant's
7 professional help, only then was he able to resolve all the issues and questions in order to complete and
8 file his mother's estate tax return, as well as his personal 2010 and 2011 tax returns, all of which were
9 completed and filed simultaneously on or around April 12, 2012. Appellant states that during this
10 entire time, his tax liability for 2010 remained intentionally overpaid so he was expecting a refund.
11 (Appeal Letter, p. 3.)

12 Appellant states that one of the cases cited by the FTB, the *Appeal of Michael J. and*
13 *Diane M. Halaburka (Halaburka)*, 85-SBE-025, decided by the Board on April 9, 1985,⁶ referenced the
14 case of *John Michael Hayes (Hayes)*, T.C. Memo. 1967-80, stating that in *Hayes*, a taxpayer was "found
15 to have reasonable cause for filing a late return when his children had pneumonia, his wife had a
16 ruptured appendix, and the taxpayer suffered a mental and physical collapse, all within five or six
17 months. In addition, all of the taxpayer's personal records necessary to complete the return were in
18 Maine while the taxpayers were in California. In this case, appellant states that it was found that the
19 taxpayer's illness and the illnesses of his family prevented him from returning to Maine to obtain the
20 documents necessary to file a return. The taxpayer thus had 'reasonable cause' for not filing." (Appeal
21 Letter, p. 3.)

22 Appellant states that, in the end, he inherited approximately \$100,000 and paid an
23 additional \$10,000 California income tax which was reported on his 2011 tax return. Appellant states
24 that any other ordinary person faced with similar circumstances and knowing that more than sufficient
25 funds had already been paid to the state would have acted similarly. Appellant attaches a Certificate of
26 Death of his mother dated December 27, 2010. (Appeal Letter, p. 3-4; attachments.)

27 _____
28 ⁶ Board of Equalization cases may be found on the Board's website: www.boe.ca.gov.

1 Respondent's Opening Brief

2 Respondent contends that it properly assessed a demand penalty against appellant for the
3 2010 tax year pursuant to Revenue and Taxation Code (R&TC) section 19133 because appellant failed
4 to respond to the Demand. Respondent asserts that the law provides that respondent may impose a
5 demand penalty when a taxpayer fails or refuses to file a return subsequent to receiving a Demand,
6 unless it is shown that such failure was due to reasonable cause and not willful neglect. Respondent
7 states that, pursuant to California Code of Regulations, title 18, section (Regulation) 19133, subdivision
8 (b), respondent will only impose the demand penalty where: (1) the taxpayer fails to timely respond to a
9 current Demand in the manner prescribed; and (2) respondent has proposed an assessment of tax under
10 the authority of R&TC section 19087, subdivision (a), after the taxpayer failed to timely respond to a
11 Request for Tax Return or a Demand in the manner prescribed, at any time during the four-taxable-year
12 period preceding the taxable year for which the current Demand is issued. (Resp. Op. Br., p. 3.)

13 Respondent states that the law provides that this penalty may be abated only if the
14 taxpayer's failure to respond is due to reasonable cause and not willful neglect and the burden of proof
15 is on the taxpayer to show that reasonable cause exists to support abatement of the penalty. Respondent
16 states that, even if the taxpayer is unaware of a filing requirement, ignorance of the law is not an excuse
17 for failing to file a timely return and each taxpayer has a personal, non-delegable obligation to file the
18 tax return by the due date, to respond to a notice and demand from respondent that a return be filed, and
19 to furnish information requested by respondent, citing the *Appeal of J. Morris and Leila G. Forbes*,
20 67-SBE-042, decided by the Board on August 7, 1967, and the *Appeal of Thomas K. and Gail G.*
21 *Boehme*, 85-SBE-134, decided by the Board on November 6, 1985. Respondent states that illness or
22 other personal difficulties which prevent a taxpayer from filing a timely return or from responding to a
23 notice and demand or request for information may be considered reasonable cause in some cases.
24 However, respondent states that if the difficulties simply cause the taxpayer to sacrifice the timeliness
25 of one aspect of the taxpayer's affairs to pursue other aspects, the taxpayer must bear the consequences
26 of that choice. Respondent states that, in order to show reasonable cause, the taxpayer must present
27 credible and competent proof that the circumstances of the illness or other personal difficulty
28 completely prevented the taxpayer from complying with the Demand, citing the *Appeal of Allen L. and*

1 *Jacqueline M. Seaman*, 75-SBE-080, decided by the Board on December 16, 1975. (Resp. Op. Br., pp.
2 3-4.)

3 In this case, respondent states that it issued an NPA for the 2010 tax year after appellant
4 failed to respond to the Demand. Furthermore, respondent states that since an NPA was also issued for
5 the 2009 tax year⁷ the Demand letter for the 2010 tax year and subsequent penalty were properly
6 imposed since the Demand for the 2010 tax year was issued within four years of the NPA for the 2009
7 tax year, satisfying Regulation 19133, as set forth above. Respondent states that appellant did not
8 respond to the Demand, and he filed his 2010 tax return on April 15, 2012, approximately one year late.
9 (Resp. Op. Br., p. 4; Exs. A & B.)

10 Respondent states that, on appeal, appellant appears to confuse the demand penalty with
11 the late filing penalty, as his argument is focused on why he was unable to timely file his tax return for
12 the 2010 tax year, not why he was unable to respond to the Demand which was sent on February 1,
13 2012. However, respondent states that the late filing penalty, which was imposed by the NPA, was
14 subsequently removed following appellant's eventual filing of his tax return. Respondent states that,
15 while respondent is sympathetic to appellant's situation, the reasons offered for appellant's failure to
16 respond to the Demand sent on February 1, 2012, well over a year following his mother's death on
17 December 27, 2010, do not establish reasonable cause. Respondent states that the documents that
18 appellant provided, including the death certificate for his mother, do not explain why appellant did not
19 respond to the Demand, which was issued to him well over a year after his mother's passing.
20 Respondent states that the law is clear that the burden of proof is on appellant to show that reasonable
21 cause exists to support abatement of the penalty. (Resp. Op. Br., p. 4; Exs. E & F.)

22 Respondent contends that appellant has failed to show why he was completely prevented
23 from complying with a Demand that was issued more than a year following his mother's death.
24 Respondent states that after appellant received the NPA on April 2, 2012, he filed his tax return a mere
25 13 days after the NPA, which suggests that appellant was not completely prevented from complying
26 with the Demand. Respondent states that appellant's argument appears to be that he was unable to
27

28 _____
⁷ For the 2009 tax year, respondent issued a Request for Tax Return dated December 28, 2010. On March 21, 2011,
respondent issued an NPA for the 2009 tax year. (Resp. Op. Br., p.4; Exs G & H.)

1 timely file his tax return for the 2010 tax year, not that he was unable to timely respond to the Demand.
2 Respondent states that appellant's appeal letter does not provide any specific detail or evidence as to
3 what steps he took after he was issued the Demand. Moreover, respondent states that it appears that
4 during the 2011 and 2012 tax years, the time period during which appellant contends he was taking care
5 of various matters following his mother's passing, appellant was still able to operate his consulting
6 business and earn a comfortable income as a result. Thus, respondent contends that reasonable cause
7 has not been demonstrated. (Resp. Op. Br., p. 4; Exs. H & I. [2011 & 2012 Wage and Income
8 Transcripts].)

9 With regard to *Halaburka, supra*, referencing *Hayes, supra*, respondent states that in
10 *Hayes*, all of the taxpayer's personal records necessary to complete the return were in Maine while the
11 taxpayers were in California, and it was determined that the taxpayer's illness and the illnesses of his
12 family prevented him from returning to Maine to obtain the documents necessary to file a return. Thus,
13 respondent states that, in that case, the taxpayer had a reasonable cause for not filing. However,
14 respondent states that appellant's case here is clearly distinguishable from the facts presented in *Hayes*
15 because the penalty at issue is the demand penalty and there is no evidence that appellant was
16 continuously prevented from responding to the Demand. Respondent states that appellant did not need
17 any documents to respond to the Demand and he did not need documents that he would need access to
18 from across the country. Respondent states that the documents needed were at his immediate disposal,
19 and there is no evidence that appellant was incapacitated on or around the February 1, 2012 period.
20 Respondent states that, while respondent sympathizes with appellant regarding the loss of his mother, it
21 cannot conclude that the death, which occurred on December 27, 2010, prevented appellant from
22 responding to the Demand issued over a year later on February 1, 2012. (Resp. Op. Br., p. 5.)

23 Appellant's Reply Brief

24 Appellant contends that the demand penalty should be abated because: (1) appellant was
25 prevented from filing his California return because essential documentation required from a third party
26 did not exist until March 29, 2012 (i.e. after the February 1, 2012 Demand to file his 2010 return by
27 March 3, 2012); (2) appellant exercised ordinary business care and prudence in attempting to comply
28 with respondent's Demand; and (3) an ordinarily intelligent and prudent businessperson would have

1 acted similarly under the circumstances. (App. Rep. Br., p. 1.)

2 Appellant states that respondent wants to dissociate the filing of appellant's 2010 tax
3 return from the Demand, even though the Demand dated February 1, 2012, clearly demands that
4 appellant file his 2010 tax return. Appellant states that his actions regarding the filing of the 2010 return
5 "a fortiori" addresses the Demand because this was a demand for a specific response, a tax return.
6 Appellant states that he responded by providing the return and the response was reasonable. Appellant
7 states that the current demand penalty relates to the late filing penalty in *Hayes*, and the facts in *Hayes*
8 are analogous to the present case, as there is evidence that appellant was prevented from responding to
9 the Demand. (App. Rep. Br., p. 1-2.)

10 Appellant states that the 2010 tax year was unique because he had to consider his
11 deceased mother's estate in his capacity as a beneficiary and, similar to the facts in the *Hayes* case
12 regarding documents not readily accessible for filing the 2010 return, appellant needed information
13 from a Schedule K-1 to competently file his 2010 return. Appellant states that this requisite Schedule
14 K-1 from a third party (his mother's estate) was not available since it did not exist until March 29, 2012
15 (after the timeframe of the Demand had expired). Appellant argues that he was also incapacitated as a
16 result of the emotional turmoil surrounding the struggle with having lost his mother which is a deep and
17 once-in-a-lifetime event. Similar to *Hayes*, appellant contends that his response was reasonable
18 because he was prevented from filing his 2010 due to the non-existence of the requisite Schedule K-1.
19 (App. Rep. Br., p. 2.)

20 Appellant contends that he filed a 2010 California personal income tax return, as the
21 Demand requested, even though he was reasonably delayed in doing so due to the missing Schedule
22 K-1. Appellant states that, even though the Demand provided that appellant could request forms or
23 additional time to file by going online or calling an automated number, there was no explicit assurance
24 in the Demand that merely contacting the FTB to request forms or additional time would in any way
25 satisfy the Demand. Moreover, appellant contends that the NPA does not list as a justification for the
26 proposed demand penalty appellant's failure to contact the FTB or failure to request additional time.
27 Rather, appellant states that the proposed demand penalty, according to the April 2, 2012 NPA, was
28 explicitly for failing to "File 2010 personal income tax return" which appellant was reasonably delayed

1 in submitting. Appellant states that the NPA did not become effective because he filed his return prior
2 to the June 1, 2012 deadline in the NPA. Appellant contends that the NPA would only become “due and
3 payable,” unless respondent received the return by June 1, 2012. Appellant states that since appellant
4 filed his 2010 tax return on April 12, 2012, the NPA did not become effective.⁸ (App. Rep. Br., pp. 2-
5 3.)

6 Appellant states that he required a Schedule K-1 to be provided to him from the estate of
7 his deceased mother, which did not exist until March 29, 2012, as evidenced by the accountant
8 statement attached as exhibit A, which states: “If applicable, you must distribute a copy of the 2011
9 K-1 to each beneficiary.” Appellant contends that this constitutes reasonable cause. (App. Rep. Br., p.
10 3; Ex. A.)

11 Appellant states that, after his mother passed on December 27, 2010, appellant correctly
12 believed that he would incur an additional state tax liability due to inheritance and acted accordingly
13 and paid an estimated inheritance tax of approximately \$10,000 for 2010 to respondent along with his
14 business related estimated tax of approximately \$10,000 for a total estimated taxes paid of \$20,000 in
15 January 2011 for the 2010 tax year. Further, appellant states that he reasonably believed that paying
16 the estimated taxes was synonymous with filing a return. Appellant states that “this logic is consistent
17 with the notion that the great state of California makes sure that it collects sufficient amounts for its
18 purse; the taxpayer can always file for a refund of overpayments, and appellant did anticipate a refund
19 for 2010.” Appellant states that “this approach avoids the likelihood of taxpayers squandering later
20 amounts that rightfully belong to the State.” Appellant states that the estimated prepayment shows
21 that appellant was not trying to evade his tax obligations; rather, appellant was attempting to anticipate
22 any tax consequences, as any reasonably prudent businessperson would do. Appellant states that the
23 death of one’s mother is a once-in-a-lifetime event which places significant, unusual, and
24 extraordinary burdens on related taxpayers. Appellant states that, even so, he provided payment
25 upfront and this overpayment of taxes, in conjunction with the state’s overall purpose of obtaining its
26

27
28 ⁸ As noted above, respondent accepted appellant’s late-filed tax return, and the NPA did not become final. The issue on
appeal is appellant’s failure to file a tax return or otherwise respond to respondent’s Demand by the March 7, 2012 deadline
stated in the Demand. By the time appellant filed his return, on April 12, 2012, the deadline for responding to the Demand
had already passed.

1 money upfront, makes a reasonable inference that this final payment of estimated taxes for 2010 was
2 synonymous with actually filing his return. (App. Rep. Br., pp. 3-4.)

3 Furthermore, appellant states that it was essential that his mother's estate first complete
4 his mother's 2010 federal tax return (after her death), followed by her federal estate return, in order for
5 the estate to then create the requisite Schedule K-1 so that appellant could then complete his 2010
6 federal tax return in that particular sequential order. However, appellant states that the requisite
7 Schedule K-1 did not, and could not, exist until his mother's federal estate return was complete. So,
8 appellant states that in 2011, he assisted his mother's estate and its executor (appellant's sister), to
9 complete and file his mother's 2010 federal tax return, which was first in the necessary sequence of tax
10 returns to be completed. Appellant states that it was then necessary for appellant to further assist his
11 mother's estate and its executor to complete his mother's 2010 estate tax return and appellant further
12 assisted the estate executor (his sister) to complete his mother's 2010 estate tax return with the help of
13 the most advanced consumer tax software available, but ultimately they concluded that both he and the
14 estate executor did not have the necessary expertise to do so. Appellant states that it should be noted
15 that he has never had to obtain any professional help to file his tax returns, and he never before had
16 attempted to assist with an estate tax return, so he could not have anticipated the difficulty of
17 completing his mother's 2010 estate tax return. (App. Rep. Br., p. 4.)

18 Appellant states that, since the executor was unable to complete the estate return, even
19 with appellant's assistance, in early 2012 appellant assisted his mother's executor in selecting and
20 hiring an accountant to complete his mother's federal estate return and thereafter create the necessary
21 Schedule K-1 and thereby enable appellant to complete his 2010 federal and state tax return. Appellant
22 states that, during the months of February to April 2012, the creation of the estate return and Schedule
23 K-1 was in the hands of the accountant and as soon as the accountant finalized his mother's federal
24 estate return and provided the estate executor with the Schedule K-1 forms for distribution, only then
25 was appellant able to complete and file both his 2010 and 2011 state tax returns, which he did in a
26 matter of days on April 12, 2012. Ultimately, appellant states that the Schedule K-1 was properly
27 reported in his 2011 state return rather than 2010, in accordance with the express information provided
28 on the K-1. Appellant states that, as the tax liability originated in 2010 and appellant had already paid

1 an estimated inheritance tax for 2010, appellant's 2010 return was reasonably delayed until he had the
2 K-1 form prior to proceeding with, completing, and filing his 2010 return. (App. Rep. Br., p. 5.)

3 Appellant contends that the sequence of tax return preparation that was required,
4 including the creation of the Schedule K-1, took several months, meaning that appellant was taking
5 reasonable steps in attempting to comply with respondent's Demand by filing his 2010 state tax return
6 long before the assessment of any penalties. Thus, appellant states that it shows that appellant was
7 acting diligently with good intentions, and not merely motivated by a potential penalty. (App. Rep. Br.,
8 p. 5.)

9 With regard to respondent's contention that appellant should have filed his 2010 state tax
10 return instead of working and attending his consulting business, appellant states that the activity of
11 attending to his consulting business was absolutely necessary and affected his livelihood. Appellant
12 states that in order to continue making a living and pay his taxes, appellant must continue to work.
13 Moreover, appellant argues that even if he did not have tax obligations, he would still have pursued this
14 activity. Thus, appellant states, he was not giving up anything, such as complying as responding to
15 respondent's Demand, to pursue these necessary activities because appellant would have done so in any
16 situation. (App. Rep. Br., p. 5.)

17 Respondent's Reply Brief

18 Respondent states that, in his reply brief, appellant argues for the first time that he was
19 prevented from filing his California return since essential documentation (in this case, the Schedule K-
20 1) required from his deceased mother's estate was not available until March 29, 2012, after the date to
21 respond to the Demand. Respondent states that this argument is without merit because a close
22 examination of exhibit A to appellant's reply brief shows that exhibit A references the Schedule K-1
23 related to the Family Trust, and significantly, is for the 2011 tax year, not the 2010 tax year on appeal.
24 Additionally, respondent states that appellant's return for the 2010 tax year, exhibit C of respondent's
25 opening brief, does not include any references to the Family Trust. Furthermore, respondent states that
26 since appellant's mother did not pass away until December 27, 2010, it is doubtful that any
27 distributions were made in 2010 related to the trust. Respondent states that, in addition, even if a K-1
28 for the 2010 tax year was needed, a prudent businessman (appellant owns his own company) would file

1 a timely return and then file an amended return at a later date following receipt of the final K-1.
2 Alternatively, respondent states that appellant could have timely responded to the Demand by having
3 made a simple phone call to respondent requesting additional time to file, which would have negated
4 the imposition of the demand penalty. (Resp. Rep. Br., pp. 1-2.)

5 Second, respondent states that appellant argues that the NPA did not become effective
6 until June 1, 2012, and thus, his filing of the return on April 15, 2012, essentially abated the
7 assessment. Respondent states that this argument is also without merit because the delayed date before
8 any billing notices go out is simply to allow a taxpayer the time to file a protest to the proposed
9 assessment or to file a return to decrease the tax and/or to ensure proper credit of any withholding.
10 Respondent states that the Demand dated February 1, 2012, stated that “If you do not respond to this
11 Demand by the reply by date indicated [March 7, 2012] and in the manner prescribed on this notice, a
12 demand penalty will be assessed at 25% of your total tax without regard to payments,” citing exhibit A
13 to respondent’s opening brief. Thus, respondent states that the Demand clearly indicated that a penalty
14 would be imposed for failure to respond, and a prudent business person would understand that failure to
15 do so or to avail himself of the option of contacting respondent to obtain additional time would result in
16 the imposition of the penalty. Therefore, respondent states that its actions must be sustained. (Resp.
17 Rep. Br., p. 2.)

18 Appellant’s Supplemental Brief

19 Appellant argues that respondent’s brief overlooks the reality of what is “reasonable”
20 cause. Appellant contends that respondent is applying an extreme perfect standard of conduct and not
21 the correct standard of an ordinary person. Appellant argues that it appears that respondent is using a
22 “perfect” businessperson test. Appellant states that the family trust is the estate of his mother of which
23 appellant is only an heir. Appellant states that respondent admits in its November 5, 2014 brief that
24 neither respondent nor appellant could have possibly known in what year and in what amounts
25 distributions were made. Appellant asserts that respondent stated: “... it is **doubtful** [emphasis added by
26 appellant] that any distributions were made in 2010 related to the trust.” In other words, appellant states,
27 neither respondent nor appellant could have known with any certainty, prior to its existence, what
28 amounts and timing of the inheritance the K-1 forms would document, and which information was

1 needed to properly file his 2010 and 2011 federal and California returns. (App. Supp. Br., pp. 1-2.)

2 Appellant argues that it is because appellant is a prudent businessman that he delayed
3 completing and filing his returns pending receipt of the requisite information to properly file his return.
4 Furthermore, appellant argues that an ordinarily intelligent and prudent businessperson would have
5 acted similarly under the circumstances, especially considering: (1) that the requisite information
6 would be documented in K-1 form(s) which appellant had not received from a third party; and (2) he
7 had already paid his estimated estate tax to the FTB. As an ordinarily intelligent and prudent
8 businessperson, appellant argues, he was motivated by the desire to avoid filing speculative, erroneous,
9 and deficient federal and California returns, such as the FTB argues, without true and correct
10 information and documentation (i.e. the K-1 form). Also, appellant states, since he expected a tax
11 refund from his estimated taxes, he had every financial incentive to complete and file his returns as
12 soon as possible. (App. Supp. Br., p. 2.)

13 Appellant contends that the perfect (and speculative) businessperson standard that
14 respondent purports, though broad, does not consider significant, once-in-a-lifetime events such as the
15 death of one's mother. Appellant asks "[h]ow much more significant, from a reasonableness and
16 objective standpoint, can one get?" Appellant states that everyone has a mother and the ordinary
17 person would likely stagger in the process of dealing with the death of their mother. Appellant states
18 that, in this case, confronted with the death of his mother, appellant was more than reasonable when he
19 overpaid his estimated inheritance taxes immediately following her death. Appellant states that, as the
20 applicable standard is an objective, reasonable standard, it should not be an "unreasonable" leap to
21 consider that when the taxpayer was confronted with this once-in-lifetime event, appellant took steps to
22 make sure his taxes were timely paid. Appellant states that this fact alone should provide sufficient
23 grounds, even from just a public policy standpoint, for abating the demand penalty in this case. (App.
24 Supp. Br., p. 2.)

25 Appellant states that the FTB further argues that the demand penalty should be imposed
26 because appellant failed "to avail him or herself of the option of contacting the respondent to **obtain**
27 [emphasis added by appellant] additional time...." Appellant states that the word "obtain" does not
28 exist in the actual Demand. Rather, appellant asserts, the express language in the Demand states: "To

1 **request** [emphasis added by appellant] forms or additional time to file go to ftb.ca.gov/inc or call our
2 automated service....” Appellant states that there is no assurance, or any language whatsoever, in the
3 Demand unequivocally stating that additional time may be “obtained.” Appellant states that, in
4 transitioning from the word “request” (additional time) in the Demand to the word “obtain” (additional
5 time) in their briefing, the FTB is performing “linguistic sleight of hand in an effort to bamboozle
6 taxpayers into paying, and the Board into upholding, otherwise unjustifiable penalties.” Furthermore,
7 appellant states that the Demand is clearly and unambiguously, as its title states, solely a “Demand for
8 Tax Return” and that it is not a demand for the taxpayer to merely contact the FTB such as, for
9 example, a “Demand for Tax Return or to Contact the FTB.” (App. Supp. Br., p. 2.)

10 Appellant states that, accordingly, in its NPA dated April 4, 2012, the FTB cites as its
11 sole justification for the imposition of the demand penalty the fact that appellant did not “File a 2010
12 California personal income tax return.” Appellant states that the NPA does not state that appellant’s
13 failure to merely contact the FTB was in any way a justification for the demand penalty to be imposed
14 on appellant and, therefore, it is disingenuous for the FTB to argue now, post facto, that the demand
15 penalty should stand because appellant failed to merely contact the FTB where that justification was not
16 cited as a basis for the penalty in the first place in the NPA. Appellant argues that his actions regarding
17 the filing of the 2010 return “a fortiori” addresses the Demand because this was a demand for a specific
18 response, a tax return. Appellant contends that it responded by providing the return and the response
19 was reasonable. (App. Supp. Br., p. 3.)

20 Applicable Law

21 California imposes a penalty for the failure to file a return or to provide information
22 upon the FTB’s demand to do so, unless reasonable cause prevented the taxpayer from responding to
23 the demand. (Rev. & Tax. Code, § 19133.) The FTB will only impose a demand penalty if the
24 taxpayer fails to respond to a current Demand and the FTB issues an NPA under the authority of R&TC
25 section 19087, subdivision (a), after the taxpayer failed to timely respond to a Request for Tax Return
26 or a Demand at any time during the four taxable years preceding the year for which the current Demand
27 is being issued. (Cal. Code Regs., tit. 18, § 19133, subd. (b).)

28 When the FTB imposes a demand penalty, the law presumes that the penalty was

1 imposed correctly, unless the taxpayer can demonstrate otherwise. (*Appeal of Yvonne M. Goodwin*,
2 97-SBE-003, Mar. 19, 1997; *Appeal of Eugene C. Findley*, 86-SBE-091, May 6, 1986.) The demand
3 penalty is designed to penalize the taxpayer's failure to respond to the notice and demand rather than a
4 failure to pay the proper tax. (*Appeal of Robert Scott*, 83-SBE-094, April 5, 1983.)

5 To establish reasonable cause, a taxpayer must show that the failure to respond to a
6 Demand occurred despite the exercise of ordinary business care. (*Appeal of Stephen C. Bieneman*,
7 82-SBE-148, July 26, 1982.) The taxpayer's reason for failing to respond must be such that an
8 ordinarily intelligent and prudent business person would have acted similarly under the circumstances.
9 (*Appeal of Robert E. Wesley and Jerry J. Couchman*, 2005-SBE-002, Nov. 15, 2005.) A taxpayer's
10 selective inability to perform tax obligations, while participating in regular business activities, does not
11 establish reasonable cause. (*Watts v. Commissioner* (1999) T.C. Memo. 1999-416.) If personal
12 difficulties simply cause the taxpayer to sacrifice the timeliness of one aspect of his affairs to pursue
13 other aspects, the taxpayer must bear the consequences of that choice. (*Appeal of William T. and Joy P.*
14 *Orr*, 68-SBE-010, Feb. 5, 1968 [involving the late filing penalty].) In *Halaburka, supra*, the taxpayers
15 failed to establish reasonable cause for failing to respond to the FTB's demand because they did not
16 show that they were continuously prevented from filing their return as a result of their child's illness
17 and the great stress they incurred.

18 STAFF COMMENTS

19 The only issue on appeal is whether appellant had reasonable cause for failing to respond
20 to the FTB's Demand. The Demand was issued on February 1, 2012, with the heading "**Demand for**
21 **Tax Return**" and stated "**You must respond by 03/07/2012.**" The Demand also provided a telephone
22 number that appellant could have used to request more time. Appellant did not reply by the March 7,
23 2012 deadline. His appeal letter states that he did not hire a professional accountant until March 21,
24 2012 (i.e., two weeks after the deadline). He did not file a tax return until April 15, 2012, which was
25 after the FTB issued an NPA, and more than one month after the deadline stated in the Demand.

26 Appellant's appeal letter argued that the delay in filing was due to his mother's illness
27 and subsequent death on December 27, 2010, a physical separation from his normal business and
28 records for periods during 2010 and 2011, and the need for him to account for estate taxes and

1 inheritance. (Appeal Letter, p. 3.) Appellant also argued that he acted reasonably in paying estimated
2 taxes based on his estimated inheritance. After respondent noted that the penalty at issue was for failing
3 to respond to its February 1, 2012 Demand, rather than for filing the tax return late, appellant's
4 representative argued that appellant did not reply to the Demand because he lacked a necessary
5 Schedule K-1 from his mother's estate to complete his 2010 taxes.⁹ When respondent noted that the
6 Schedule K-1 was for 2011, rather than the 2010 year at issue, appellant's representative argued that
7 appellant needed to wait for the completion of his mother's estate tax return so that he could receive a
8 Schedule K-1 in order to prepare his taxes.¹⁰ Appellant's representative also argued that appellant could
9 not have known if any distributions were made from his mother's estate during 2010 after his mother's
10 death on December 27, 2010.¹¹

11 At the hearing, appellant will want to focus on the actions he took between February 1,
12 2012, when the Demand was issued, and March 7, 2012, when a reply was required. Appellant will
13 need to demonstrate that his actions or inactions were consistent with those that would have been taken
14 (or not taken) by an ordinarily intelligent and prudent business person in his circumstances who
15 received a Demand for a tax return from the FTB. Appellant will want to address whether a prudent
16 business person would have contacted the FTB prior to the deadline stated in the Demand and asked for
17 an extension so that he could obtain any needed information. He will also want to address whether he
18 acted prudently in not engaging a professional accountant prior to March 21, 2012, when he received
19 the Demand on or about February 1, 2012, and the Demand required a response by March 7, 2012. To
20 the extent appellant argues that his failure to timely respond to the Demand was reasonable because he
21

22 _____
23 ⁹ Appellant states in his appeal letter that, with the help of the accountant he hired on March 21, 2012, he was he able to
24 complete and file his mother's estate tax return as well as his personal 2010 and 2011 tax returns. Appellant will want to
25 address at the hearing whether the lack of a Schedule K-1 was due to the fact he did not engage an accountant until March 21,
26 2012.

27 ¹⁰ Appellant should be prepared to clarify whether his mother's estate required the filing of an estate tax return. Exhibit A to
28 appellant's reply brief indicates that a 2011 fiduciary return (Form 1041) was filed on March 29, 2012, but there is no
documentation of an estate tax return for any year or any indication of a fiduciary income tax return for 2010. For the year at
issue, California did not impose an estate tax, and federal estate taxes generally only applied to estates of over \$5 million.

¹¹ As appellant's sister was the executor of his mother's estate, and appellant asserts that he was directly involved in the
filing of the tax returns for the estate, appellant should be prepared to address whether he could have asked his sister
regarding the timing of any distributions made by his mother's estate.

1 believed he had paid all his taxes, he should be prepared to address the authorities noting that the
2 demand penalty penalizes the failure to respond to a Demand, rather than any failure to pay tax. (See,
3 e.g., *Appeal of Robert Scott, supra*; *Appeal of Yvonne M. Goodwin, supra*; *Appeal of W.L. Bryant,*
4 *83-SBE-180, Aug. 17, 1983.*)

5 In the event either party has additional evidence to provide, such evidence should be
6 provided to the Board Proceedings Division at least 14 days prior to the oral hearing, pursuant to
7 California Code of Regulations, title 18, section 5523.6.¹²

8 ///

9 ///

10 ///

11 CohenM_jl

12

13

14

15

16

17

18

19

20

21

22

23

24

25

26

27

28 ¹² Evidence exhibits should be sent to: Khaaliq Abd'Allah, Appeals Analyst, Board Proceedings Division, State Board of
Equalization, P.O. Box 942879 MIC:80, Sacramento, California, 94279-0080.