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7 **BOARD OF EQUALIZATION**  
8 **STATE OF CALIFORNIA**

10 In the Matter of the Appeal of: ) **HEARING SUMMARY**  
11 ) **PERSONAL INCOME TAX APPEAL**  
12 **CLOVUS M. SYKES** ) Case No. 817237<sup>1</sup>

	<u>Year</u>	<u>Proposed Assessment Additional Tax</u>	<u>Penalties and Fee<sup>2</sup></u>
	2011	\$5,349.00	\$2,752.50

17 Representing the Parties:

18 For Appellant: Clovus M. Sykes  
19 For Franchise Tax Board: Brian Werking, Tax Counsel

21 **QUESTIONS:** (1) Whether appellant has demonstrated error in the Franchise Tax Board’s (FTB or  
22 respondent) proposed assessment of additional tax;  
23 (2) Whether appellant has shown reasonable cause for failing to timely file;  
24 (3) Whether appellant has shown reasonable cause for failing to reply to the FTB’s  
25 Demand for Tax Return (Demand);

27 <sup>1</sup> This appeal was originally scheduled for the Board’s May 27-28, 2015 oral hearing calendar. Appellant requested a  
28 postponement due to a scheduling conflict, and the matter was rescheduled to the July 28-29 oral hearing calendar.

<sup>2</sup> This amount consists of: (1) a late filing penalty of \$1,337.25; (2) a notice and demand penalty (i.e., failure to file upon  
demand penalty) of \$1,337.25; and (3) a filing enforcement fee of \$78.00. (Resp. Op. Br., p. 1.)

1 (4) Whether the filing enforcement fee may be abated; and

2 (5) Whether the Board should impose a frivolous appeal penalty.<sup>3</sup>

3  
4 HEARING SUMMARY

5 Background

6 Respondent's Integrated Non-Filer Compliance (INC) program annually matches  
7 income records obtained from various reporting sources against filed tax returns to identify individuals  
8 who may not have fulfilled the legal requirement to file a California income tax return. As an  
9 important part of the INC program, respondent receives information regarding payments made to  
10 California residents that are reported on federal information returns (federal Form 1099 series) by the  
11 payers of such income. (Resp. Op. Br., p. 1.)

12 For the 2011 tax year, respondent obtained information from reporting sources which  
13 indicated that appellant received income sufficient to prompt a return-filing requirement.<sup>4</sup> When  
14 appellant failed to file a 2011 California income tax return, respondent mailed a Demand on January 16,  
15 2013, requiring appellant to respond by February 20, 2013, either by filing a 2011 return or explaining  
16 why a 2011 return was not required. Because appellant did not file a 2011 return or explain why a 2011  
17 return was not required, respondent issued a Notice of Proposed Assessment (NPA) on September 16,  
18 2013. On the NPA, respondent proposed an assessment of additional tax of \$5,349.00, a late filing  
19 penalty of \$1,337.25, a notice and demand (demand) penalty of \$1,337.25, and a filing enforcement fee  
20

21  
22 <sup>3</sup> Appellant has not filed a valid California income tax return for any tax year since 1995. Respondent issued filing  
23 enforcement NPAs against appellant for the 2000 through 2011 tax years. The NPAs for 2000 through 2010 are final, and  
24 the NPA for 2011 is being protested. This is appellant's sixth appeal of this nature. Appellant filed appeals for tax years  
25 2001 (Case No. 492696) and 2004 (Case No. 492702), which were consolidated, and in which the Board found against  
26 appellant and imposed frivolous appeal penalties of \$375 for 2001 and \$375 for 2004. Appellant then filed a petition for  
27 rehearing, which was denied on September 14, 2010. Appellant filed an appeal for tax year 2006 (Case No. 512493) in  
28 which the Board found against appellant and imposed a frivolous appeal penalty of \$750. Appellant then filed a petition for  
rehearing, which was denied on December 14, 2010. Appellant filed an appeal for tax year 2007 (Case No. 529645) in  
which the Board found against appellant and imposed a frivolous appeal penalty of \$2,500. Appellant then filed a petition  
for rehearing, which was denied on June 21, 2011. Appellant filed an appeal for tax year 2009 (Case No. 790625) in which  
the Board found against appellant and imposed a frivolous appeal penalty of \$5,000.

<sup>4</sup> For the 2011 tax year, a single individual under age 65 with no dependents realizing a California gross income of \$15,152  
or a California adjusted gross income of \$12,122 was required to file a California income tax return. (Resp. Op. Br., p. 2.)

1 of \$78.00, plus interest. Respondent based the NPA tax calculation on total income of \$87,669.<sup>5</sup> (Resp.  
2 Op. Br., p. 2, Ex. A; Appeal Letter, Ex. D.)

3 Respondent received a timely protest letter dated November 15, 2013, that included a  
4 request for a hearing. The requested protest hearing was conducted on March 27, 2014, at respondent's  
5 Sacramento District Office. After a complete review of appellant's protest, respondent issued a Notice  
6 of Determination on April 15, 2014, which stated that the NPA would be affirmed. On May 5, 2014,  
7 respondent issued a Notice of Action (NOA) affirming the NPA. This timely appeal followed. (Resp.  
8 Op. Br., p. 2, Ex. B; Appeal Letter, Exs. A & B.)

9 Appellant's Contentions

10 Appellant states that he had "payee status" during 2011. Appellant states that he was  
11 domiciled and performed services in California. Appellant states that he is not a resident, nonresident,  
12 or part-year resident. Appellant states that no taxable payments were made to him in 2011 and the  
13 payments he received from "payors" were inappropriately reported to the Internal Revenue Service  
14 (IRS) and the FTB. Appellant states that the FTB's calculation of his taxable income is based on the  
15 unauthorized disclosure of the payment amounts. Appellant states that third-party information reported  
16 to the FTB is hearsay. Appellant states that his due process rights were abridged. Appellant states that  
17 respondent purposely obstructed his right to satisfy his burden of proof and respondent's determination  
18 does not comply with federal or California tax law. Appellant states that respondent does not have the  
19 authority to determine appellant's filing status. Appellant states that he has rebutted respondent's  
20 presumption of correctness. Appellant states that he sent the FTB a corrected Form 1099-MISC issued  
21 by Juanita Woods, a third-party payor, that excludes \$11,397 of erroneously reported payments.  
22 Appellant attaches a "corrected" Form 1099 and a letter allegedly from Ms. Woods stating that the  
23 payment was erroneously reported. (Appeal Letter, pp. 2, 6, & 22; App. Rep. Br., pp. 3-4, Ex. A; App.  
24 Supp. Br., pp. 2, 3, 10, & 16.)

25  
26  
27 <sup>5</sup> The \$87,669 of income includes: (1) \$67,115 reported on a Form 1099-MISC from Hunter Johnson & Associates;  
28 (2) \$11,397 reported on a Form 1099-MISC from Juanita Woods; (3) \$6,265 reported on a Form 1099-R from California  
Public Employees Retirement System; (4) \$1,132 reported on a Form 1099-MISC from David Craft; (5) \$1,050 reported on a  
Form 1099-MISC from Health Net of California Inc.; and (6) \$710 reported on a Form 1099-MISC from Jack L. Hunter.  
(Resp. Op. Br., p. 2.)

1           Respondent's Contentions

2           Respondent states that appellant refuses to file a 2011 return for which he is legally  
3 obligated and attempts, through the assertion of frivolous arguments, to avoid a tax for which he is  
4 clearly liable.<sup>6</sup> Respondent states that, over the years, the Board, the courts, the IRS, and respondent  
5 have consistently and emphatically rejected arguments similar to appellant's and have found such  
6 arguments to be frivolous and without any significant merit. (Resp. Op. Br., p. 4.)

7           Respondent states that appellant has not met his burden of proof by contradicting  
8 respondent's proposed assessment with any specific, credible, or relevant information. Respondent  
9 states that, because appellant has failed to file a valid 2011 return and did not provide respondent or the  
10 Board with any specific income information relating to his 2011 income, he is not in a good position to  
11 criticize the NPA issued by respondent, citing the *Appeals of Fred R. Dauberger, et al.*, 82-SBE-082,  
12 decided by the Board on March 31, 1982.<sup>7</sup> Respondent states that the Board has no jurisdiction to hear  
13 appellant's arguments regarding alleged violations of substantive or procedural rights, citing California  
14 Code of Regulations, title 18, section (Regulation) 5412, subdivision (b). (Resp. Op. Br., p. 4.)

15           Respondent states that appellant has never denied receiving the income reported on  
16 Forms 1099-MISC, reportedly paid to him in 2011. Respondent states that appellant has not attempted  
17 to demonstrate any error in respondent's proposed assessment of additional tax, penalties, and interest  
18 for his 2011 tax year. Respondent states that its initial burden is to show that the proposed assessment is  
19 reasonable and rational and, if respondent satisfies this burden, the proposed assessment is presumed to  
20 be correct, and the burden of proof falls upon appellant. Respondent states that it has provided a  
21 reasonable foundation for the proposed assessment, linking appellant to unreported income from Forms  
22 1099-MISC and a Form 1099-R.<sup>8</sup> Respondent states that the use of this source of income information as

23 \_\_\_\_\_  
24  
25 <sup>6</sup> Respondent states that, according to federal records, appellant has not filed a federal income tax return for the 2011 tax  
year. (Resp. Op. Br., p. 3; Ex. C.)

26 <sup>7</sup> Board of Equalization cases (designated "SBE") may generally be found at: [www.boe.ca.gov](http://www.boe.ca.gov)

27 <sup>8</sup> Respondent states that appellant's federal Wage and Income Transcript reflects the income information as shown on the  
28 NPA. Respondent notes that the transcript reflects income that respondent did not know about when it issued the NPA and  
consists of \$78 from Aviva Life & Annuity Company. Respondent states that it will not reissue the NPA to include this  
income at this time. (Resp. Op. Br., p. 4, Ex. E.)

1 a basis for the 2011 proposed assessment is both rational and reasonable, and respondent has met its  
2 initial burden. (Resp. Op. Br., p. 4.)

3 Respondent states that appellant submits a “corrected” Form 1099-MISC, purportedly  
4 from Ms. Woods, which revises the reported amount of non-employee compensation paid to appellant  
5 from \$11,397 to zero. Respondent states that appellant provides an unsigned document that purports to  
6 be a letter from Ms. Woods, explaining the reasoning for issuing the corrected Form 1099-MISC to  
7 appellant. Respondent states that the author of that document explains that the payor, Ms. Woods,  
8 recently became aware that she was not required to report payments made to payees who are  
9 United States persons performing services under independent contract agreements and, therefore, she is  
10 issuing a corrected Form 1099-MISC that omits the payments made to appellant for the 2011 tax year.  
11 (Resp. Rep. Br., p. 1; App. Rep. Br., Ex. A.)

12 Respondent states that the author of the document bases his or her position on Treasury  
13 Decision 8734, which is related to the withholding of tax of nonresident aliens under Internal Revenue  
14 Code (IRC) section 1441. Respondent states that IRC section 1441 is not relevant because it addresses  
15 the requirements for the withholding of tax on nonresident aliens and does not address informational  
16 reporting requirements for payors that make payments to payees who are United States persons  
17 performing services under independent contract agreements. Respondent states that the payments made  
18 by Ms. Woods to appellant were required to be reported under IRC section 6041, which requires payors  
19 of over \$600 in the course of a trade or business during a tax year to file information returns (Form  
20 1099) to report those payments. (Resp. Rep. Br., p. 2.)

21 Respondent states that appellant has not provided any information to show that he is not  
22 a resident and that appellant lives and works in California. With respect to the late filing penalty,  
23 respondent states that the penalty was imposed properly pursuant to R&TC section 19131 and that  
24 appellant fails to demonstrate reasonable cause for failing to timely file. Respondent states that the  
25 demand penalty was imposed properly pursuant to R&TC section 19133, which requires that  
26 respondent propose an assessment of tax after the taxpayer failed to timely respond to a Request for  
27 Tax Return (Request) or a Demand at any time during the four taxable years preceding the taxable  
28 year for which the current Demand is issued. Respondent states that it previously issued Demands and

1 NPAs for the 2000 through 2011 tax years. Respondent states that appellant has not presented  
2 evidence of reasonable cause to support an abatement of the demand penalty. Respondent states that  
3 the filing enforcement fee was imposed properly pursuant to R&TC section 19254 and that there is no  
4 reasonable cause exception to the fee. (Resp. Op. Br., pp. 4-5, Ex. G.)

5 Applicable Law

6 Proposed Assessment

7 R&TC section 17041 imposes a tax “. . . upon the entire taxable income of every  
8 resident of this state . . .” R&TC section 18501 requires every individual subject to the Personal  
9 Income Tax to make and file a return with the FTB “stating specifically the items of the individual’s  
10 gross income from all sources and the deductions and credits allowable . . .” R&TC section 19087,  
11 subdivision (a), provides:

12 If any taxpayer fails to file a return, or files a false or fraudulent return with intent to  
13 evade the tax, for any taxable year, the Franchise Tax Board, at any time, may require a  
14 return or an amended return under penalties of perjury or may make an estimate of the net  
15 income, from any available information, and may propose to assess the amount of tax,  
16 interest, and penalties due.

17 If the FTB makes a tax assessment based on an estimate of income, the FTB’s initial  
18 burden is to show why its assessment is reasonable and rational. (*Todd v. McColgan* (1949)  
19 89 Cal.App.2d 509; *Appeal of Michael E. Myers*, 2001-SBE-001, May 31, 2001.) Federal courts have  
20 held that the taxing agency need only introduce some evidence linking the taxpayer with the unreported  
21 income. (See *Rapp v. Commissioner* (9th Cir. 1985) 774 F.2d 932.) When a taxpayer fails to file a  
22 valid return, respondent’s use of income information from various sources to estimate a taxpayer’s  
23 taxable income is a reasonable and rational method of estimating taxable income. (See *Palmer v.*  
24 *Internal Revenue Service* (9th Cir. 1997) 116 F.3d 1309, 1313; *Andrews v. Commissioner*, T.C. Memo.  
25 1998-316; *Giddio v. Commissioner* (1970) 54 T.C. 1530, 1533; *Appeals of Walter R. Bailey*,  
26 92-SBE-001, Feb. 20, 1992; *Appeal of R. and Sonja J. Tonsberg*, 85-SBE-034, Apr. 9, 1985.)

27 Once the FTB has met its initial burden, the assessment is presumed correct and the  
28 taxpayer has the burden of proving it to be wrong. (*Todd v. McColgan, supra*; *Appeal of*  
*Michael E. Myers, supra*.) Unsupported assertions are not sufficient to satisfy a taxpayer’s burden of

1 proof. (*Appeal of Aaron and Eloise Magidow*, 82-SBE-274, Nov. 17, 1982.) In the absence of  
2 uncontradicted, credible, competent, and relevant evidence showing error in the FTB’s determinations,  
3 respondent’s proposed assessments must be upheld. (*Appeal of Oscar D. and Agatha E. Seltzer*,  
4 80-SBE-154, Nov. 18, 1980.) A taxpayer’s failure to produce evidence that is within his control gives  
5 rise to a presumption that such evidence is unfavorable to his case. (*Appeal of Don A. Cookston*,  
6 83-SBE-048, Jan. 3, 1983.)

#### 7 Residency

8 California residents are taxed upon their entire taxable income (regardless of source),  
9 while nonresidents are only taxed on income from California sources. (Rev. & Tax. Code, § 17041,  
10 subs. (a), (b), and (i); Rev. & Tax. Code, § 17951.) Part-year residents are taxed on their income  
11 earned while residents of this state, as well as all income derived from California sources. (Rev. &  
12 Tax. Code, § 17041, subs. (b) & (i).) R&TC section 17014, subdivision (a), provides that the term  
13 “resident” includes: (1) every individual who is in California for other than a temporary or transitory  
14 purpose; and (2) every individual domiciled in California who is outside California for a temporary or  
15 transitory purpose. Thus, an individual domiciled in California remains a resident until he leaves for  
16 other than a temporary or transitory purpose. (Cal. Code Regs., tit. 18, § 17014; see also Rev. & Tax.  
17 Code, § 17014.) The FTB’s determination of residency is presumptively correct. (*Appeals of*  
18 *John R. Young*, 86-SBE-199, Nov. 19, 1986.)

#### 19 Constitutional/Due Process Issues

20 The Board is precluded from determining the constitutional validity of California  
21 statutes, and has an established policy of declining to consider constitutional issues. (Cal. Const.,  
22 art. III, § 3.5; *Appeal of Aimor Corp.*, 83-SBE-221, Oct. 26, 1983; *Appeals of Walter R. Bailey, supra.*)  
23 In *Bailey, supra*, the Board stated:

24 [D]ue process is satisfied with respect to tax matters so long as an opportunity is given to  
25 question the validity of a tax at some stage of the proceedings. It has long been held that  
26 more summary proceedings are permitted in the field of taxation because taxes are the  
27 lifeblood of government and their prompt collection is critical.

#### 27 Late Filing Penalty

28 R&TC section 19131 provides that a late filing penalty shall be imposed when a

1 taxpayer fails to file a tax return on or before its due date, unless the taxpayer establishes that the late  
2 filing was due to reasonable cause and not due to willful neglect. When the FTB imposes a late filing  
3 penalty, the law presumes that the penalty was imposed correctly. (*Todd v. McColgan, supra; Appeal of*  
4 *Yvonne M. Goodwin, 97-SBE-003, Mar. 19, 1997.*) To establish reasonable cause, a taxpayer must  
5 show that the failure to file a return occurred despite the exercise of ordinary business care. (*Appeal of*  
6 *Howard G. and Mary Tons, 79-SBE-027, Jan. 9, 1979; Appeal of Stephen C. Bieneman, 82-SBE-148,*  
7 *July 26, 1982.*) The taxpayer's reason for failing to file must be such that an ordinarily intelligent and  
8 prudent businessperson would have acted similarly under the circumstances. (*Appeal of Joseph W. and*  
9 *Elsie M. Cummings, 60-SBE-040, Dec. 13, 1960.*)

#### 10 Demand Penalty

11 California imposes a penalty for the failure to file a return or to provide information  
12 upon the FTB's demand to do so, unless reasonable cause prevented the taxpayer from responding to  
13 the Demand. (Rev. & Tax. Code, § 19133.) The FTB will only impose a demand penalty if the  
14 taxpayer fails to respond to a current Demand and the FTB issues an NPA under the authority of R&TC  
15 section 19087, subdivision (a), after the taxpayer failed to timely respond to a Request or a Demand at  
16 any time during the four taxable years preceding the year for which the current Demand is being issued.  
17 (Cal. Code Regs., tit. 18, § 19133, subd. (b).) When the FTB imposes a demand penalty, the law  
18 presumes that the penalty was imposed correctly. (*Todd v. McColgan, supra; Appeal of*  
19 *Yvonne M. Goodwin, supra.*) The burden is on the taxpayer to prove that reasonable cause prevented  
20 him from responding to the Demand. (*Appeal of Kerry and Cheryl James, 83-SBE-009, Jan. 3, 1983.*)  
21 To establish reasonable cause, a taxpayer must show that the failure to respond to a Demand occurred  
22 despite the exercise of ordinary business care. (*Appeal of Stephen C. Bieneman, supra.*) The  
23 taxpayer's reason for failing to respond must be such that an ordinarily intelligent and prudent  
24 businessperson would have acted similarly under the circumstances. (*Appeal of Joseph W. and*  
25 *Elsie M. Cummings, supra.*)

#### 26 Filing Enforcement Fee

27 R&TC section 19254 provides that if the FTB mails a formal legal Demand to a  
28 taxpayer, a filing enforcement cost recovery fee is required to be imposed when the taxpayer fails or

1 refuses to file the return within the 25-day period. (Rev. & Tax. Code, § 19254, subd. (a)(2).) Once  
2 properly imposed, there is no provision in the Revenue and Taxation Code which would excuse the  
3 FTB from imposing the filing enforcement cost recovery fee for any circumstances, including  
4 reasonable cause. (Rev. & Tax. Code, § 19254.)

#### 5 Frivolous Appeal Penalty

6 The Board may impose a penalty of up to \$5,000 whenever it appears to the Board that  
7 proceedings before it have been instituted or maintained primarily for delay or that the position is  
8 frivolous or groundless. (Rev. & Tax. Code, § 19714; Cal. Code Regs., tit., 18, § 5454.) The following  
9 factors are considered in determining whether, and in what amount, to impose the penalty: (1) whether  
10 the taxpayer is making arguments that have been previously rejected by the Board in a Formal Opinion  
11 or by courts; (2) whether the taxpayer is repeating arguments that he made in prior appeals; (3) whether  
12 the taxpayer filed the appeal with the intent of delaying legitimate tax proceedings or the legitimate  
13 collection of tax owed; and (4) whether the taxpayer has a history of filing frivolous appeals or failing  
14 to comply with California's tax laws. (Cal. Code Regs., tit. 18, § 5454.) The Board may consider other  
15 relevant factors in addition to the factors listed above. (Cal. Code Regs., tit. 18, § 5454.) A taxpayer's  
16 prior pattern and practice of conduct is relevant when determining whether to impose a frivolous appeal  
17 penalty and in what amount. (*Appeal of Alfons Castillo*, 92-SBE-020, July 20, 1992.)

#### 18 STAFF COMMENTS

19 At the hearing, appellant should be prepared to provide evidence which demonstrates  
20 error in the respondent's determination and reasonable cause to abate the late filing and demand  
21 penalties. It appears that respondent has provided a reasonable foundation for the proposed assessment,  
22 based on income information from federal Forms 1099. The Board previously concluded that methods  
23 of estimating income like this are rational and reasonable and, thus, the burden of proof has shifted to  
24 appellant in this matter. Appellant has not provided any evidence demonstrating error in respondent's  
25 proposed assessment or any reasonable cause to abate the late filing or demand penalties. Pursuant to  
26 Rules for Tax Appeals Regulation 5523.6, appellant should provide any additional evidence in support

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Appeal of Clovus M. Sykes

**NOT TO BE CITED AS PRECEDENT** - Document prepared for  
Board review. It does not represent the Board's decision or opinion.

1 of his position to the Board Proceedings Division at least 14 days prior to the oral hearing.<sup>9</sup>

2           Regarding appellant's contention that the income from Juanita Woods is not taxable,  
3 staff notes that the income was properly reported pursuant to IRC section 6014(a), which requires that  
4 taxpayers who are engaged in a trade or business file an information return, generally a Form 1099-  
5 MISC, if a payment of \$600 or more is made to an independent contractor. Staff also notes that  
6 Treasury Decision 8734 is not applicable because it relates to the withholding of tax on nonresident  
7 aliens. Additionally, it appears to staff that the letter and the "corrected" Form 1099-MISC from  
8 Ms. Woods were created by appellant and not Ms. Woods as alleged (e.g., the handwriting on the Form  
9 1099 matches appellant's handwriting of the exhibit number at the bottom of the page), though the  
10 income would be taxable to appellant regardless of the validity of those documents.

11           Additionally, both parties should be prepared to discuss whether, and in what amount, a  
12 frivolous appeal penalty should be imposed, as the Board has the authority under the Revenue and  
13 Taxation Code to determine whether, and in what amount, to impose such a penalty. Appellant's  
14 arguments, such as: (1) respondent violated his due process rights; (2) respondent does not have the  
15 authority to propose the assessment; and (3) the income information received by the FTB is "hearsay",  
16 are the types of arguments that have been consistently rejected by the IRS, the federal courts,  
17 respondent, and the Board, for many years. (See, e.g., *Appeal of Michael E. Myers, supra*; *Appeal of*  
18 *Fred R. Dauberger, et al., supra*; *Appeal of Alfons Castillo, supra*; *Appeals of Walter R. Bailey, supra*;  
19 *Appeals of Robert E. Wesley, et al., 2005-SBE-002, Nov. 15, 2005.*) Appellant was notified in the 2011  
20 NOA and in a letter from Board staff dated July 1, 2014, that the Board may impose a frivolous appeal  
21 penalty.

22           Based upon the facts and circumstances present in this appeal, it appears to staff that the  
23 Board may wish to consider a frivolous appeal penalty of \$5,000. However, whether, and in what  
24 amount, to impose this penalty is entirely in the Board's discretion under Regulation 5454 of the  
25 Board's Rules for Tax Appeals.

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<sup>9</sup> 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.