

1 John O. Johnson
 Tax Counsel
 2 Board of Equalization, Appeals Division
 450 N Street, MIC:85
 3 PO Box 942879
 Sacramento CA 95814
 4 Tel: (916) 319-9118
 Fax: (916) 324-2618
 5

6 Attorney for the Appeals Division

7 **BOARD OF EQUALIZATION**

8 **STATE OF CALIFORNIA**

9
 10 In the Matter of the Consolidated Appeals of:) **HEARING SUMMARY**
 11) **PERSONAL INCOME TAX APPEAL**
 12 **CLOVUS M. SYKES**¹) Case Nos. 492696, 492702
 13)

| | <u>Years</u> | <u>Proposed Assessments</u> ² | |
|--|--------------|--|-------------------------------|
| | | <u>Tax</u> | <u>Penalties</u> ³ |
| | 2001 | \$2,686.00 | \$1,623.68 |
| | 2004 | \$2,831.00 | \$ 707.75 |

17 Representing the Parties:

18 For Appellant: Clovus M. Sykes

19 For Franchise Tax Board: Jane Perez, Tax Counsel

- 20
 21 **QUESTIONS:** (1) Whether appellant has demonstrated error in the underlying tax assessment.
 22 (2) Whether appellant has shown reasonable cause for the abatement of penalties.
 23 (3) Whether the Board should impose a frivolous appeal penalty.
 24

25 ¹ Appellant resides in Sacramento County, California.

26 ² Respondent should be prepared to provide the amount of interest accrued as of the date of the oral hearing.

27 ³ The penalty amount for 2001 consists of a \$671.50 late filing penalty, a \$280.68 post-amnesty penalty, and a \$671.50
 28 demand penalty. Respondent concedes the demand penalty on appeal for 2001. (Resp. Op Br., Case No. 492696, p. 1, fn. 1.)
 The penalty amount for 2004 is a late filing penalty. (Resp. Op. Br., Case No. 492702, p. 4.)

1 HEARING SUMMARY

2 Background

3 2001

4 On August 12, 2008, appellant filed California income tax returns for 2001 and 2004.
5 For 2001, appellant reported zero taxable income and requested a refund of \$133 for withholding and
6 excess SDI credits. (Resp. Op. Br., Case No. 492696, exhibit A.) After reviewing the return,
7 respondent issued a Notice of Proposed Assessment (NPA) for the 2001 tax year on September 15,
8 2008. (Appeal Letter, Case No. 492696, exhibits.) The NPA proposed an unpaid tax liability of
9 \$2,686.00, a late filing penalty of \$671.50, a post-amnesty penalty of \$280.68, and applicable interest.⁴
10 Respondent indicates that it based the NPA on information it received from the California Department
11 of Insurance (CDI) through its Integrated Non-Filer Compliance (INC) program. (Resp. Op. Br., Case
12 No. 492696, pp. 1-2.) The information from the CDI showed that appellant has been an insurance agent
13 since 1994. (*Id.* at exhibit C.) Respondent used the calculated average business income of insurance
14 agents, adjusted by the California Consumer Price Index change for 2001, to reach an estimated income
15 for appellant. (*Id.* at p. 2.) Respondent sent a letter to appellant on September 26, 2008, stating that
16 appellant's return was a frivolous return and demanding that appellant file a valid 2004 tax return within
17 30 days. (*Id.* at exhibit B.)

18 Appellant protested the NPA and requested an oral protest hearing. (Resp. Op. Br., Case
19 No. 492696, exhibit D.) Respondent acknowledged appellant's protest by letter dated January 20, 2009,
20 and informed appellant that it would schedule an oral hearing. (*Id.* at exhibit E.) On March 30, 2009,
21 respondent issued a Notice of Oral Hearing on Protest to appellant with the date and location of the
22 protest hearing. (*Id.* at exhibit F.) Appellant attended the protest hearing. On May 11, 2009, respondent
23 affirmed the NPA by issuing the Notice of Action (NOA) for 2001, based on the hearing officer's
24 recommendation. (Appeal Letter, Case No. 492696, exhibits.) This timely appeal followed.

25 2004

26 On August 12, 2008, appellant filed California income tax returns for 2001 and 2004.
27

28 ⁴ The 2001 NPA also imposed a \$671.50 demand penalty that respondent concedes on appeal. (Resp. Op. Br., Case No. 492696, p. 1, fn. 1.)

1 Appellant reported zero taxable income for 2004. (Resp. Op. Br., Case No. 492702, Exhibit A.) After
2 reviewing the return, respondent sent a letter to appellant on September 15, 2008, stating that the return
3 was a frivolous return and demanding that appellant file a valid 2004 tax return within 30 days. (*Id.* at
4 exhibit B.) Respondent issued a NPA for the 2004 tax year on September 22, 2008. (Appeal Letter,
5 Case No. 492702, exhibits.) The NPA proposed an unpaid tax liability of \$2,831.00, a late filing penalty
6 of \$707.75, and applicable interest. Respondent indicates that it based the NPA on information it
7 received from the CDI through its INC program. (Resp. Op. Br., Case No. 492702, pp. 1-2.) The
8 information from the CDI showed that appellant has been an insurance agent since 1994. (*Id.* at exhibit
9 C.) Respondent used the calculated average business income of insurance agents, adjusted by the
10 California Consumer Price Index change for 2004, to reach an estimated income for appellant. (*Id.* at p.
11 2.)

12 Appellant protested the NPA and requested an oral protest hearing. (Resp. Op. Br., Case
13 No. 492702, exhibit D.) Respondent acknowledged appellant's protest by letter dated January 20, 2009,
14 and informed appellant that it would schedule an oral hearing. (*Id.* at exhibit E.) On March 30, 2009,
15 respondent issued a Notice of Oral Hearing on Protest to appellant with the date and location of the
16 protest hearing. (*Id.* at exhibit F.) Appellant attended the protest hearing. On May 11, 2009, respondent
17 affirmed the NPA by issuing the NOA for 2004, based on the hearing officer's recommendation.
18 (Appeal Letter, Case No. 492702, exhibits.) This timely appeal followed.

19 Contentions

20 Appellant sets forth the following contentions:

- 21 • Appellant is a "citizen of the United States," but not an "individual," "resident," or
22 "person" for the purposes of the Internal Revenue Code (IRC). (Appeal Letter, Case No.
23 492702, pp. 2-3.)
- 24 • Appellant is excluded by definition from the proposed taxation and the requirement to
25 file returns for the appeal years. (App. Reply Br., Case No. 492702, pp. 15-18 & 21.)
- 26 • Respondent's estimation of income does not comply with federal law. (*Id.* at p. 13.)
- 27 • Respondent has not shown how appellant's return, reporting zero total income, is
28 incorrect. (*Id.* at p. 9.)

- 1 • The penalties should be abated because appellant has no taxable income upon which to
2 levy penalties. (*Id.* at p. 23.)
- 3 • Respondent cannot show that the frivolous appeal penalty should apply. (*Id.* at p. 27.)
- 4 • California Taxing Authorities (CTA) have committed procedural errors against appellant.
5 (Appeal Letter, Case No. 492702, p. 4.)

6 Respondent contends that appellant's returns reporting zero income are not valid returns,
7 and that his arguments on appeal are frivolous attempts to avoid a tax for which he is clearly liable.
8 (Resp. Op. Br., Case No. 429702, p. 2.) Respondent asserts that appellant's contentions have been
9 previously found by the Board, the courts, the IRS, and respondent to be frivolous arguments without
10 merit, and therefore a frivolous appeal penalty should apply. (*Ibid.*)

11 Respondent contends that appellant has a filing obligation for 2001 and 2004, appellant
12 failed to submit valid returns, respondent proposed an assessment for each year based on properly
13 estimated income, and appellant has failed to provide information showing respondent's determinations
14 are erroneous. (Resp. Op. Br., Case No. 429702, pp. 3-4.) Respondent concedes the demand penalty for
15 2001, and asserts that the late filing penalties are properly imposed. (Resp. Op. Br., Case No. 492696,
16 pp. 4-5.)

17 Applicable Law

18 Revenue and Taxation Code (R&TC) section 17041 imposes a tax “. . . upon the entire
19 taxable income of every resident of this state . . .” and “. . . upon the entire taxable income of every
20 nonresident or part-year resident which is derived from sources in this state . . .” R&TC section 18501
21 requires every individual subject to the Personal Income Tax to make and file a return with respondent
22 “stating specifically the items of the individual’s gross income from all sources and the deductions and
23 credits allowable . . .” R&TC section 19087, subdivision (a), provides:

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

29 If respondent makes a tax assessment based on an estimate of income, respondent’s initial
30 burden is to show why its assessment is reasonable and rational. (*Todd v. McColgan* (1949) 89

1 Cal.App.2d 509; *Appeal of Michael E. Myers*, 2001-SBE-001, May 31, 2001.) Federal courts have held
2 that the taxing agency need only introduce some evidence linking the taxpayer with the unreported
3 income. (See *Rapp v. Commissioner* (9th Cir. 1985) 774 F.2d 932.) Respondent's use of income
4 information from agencies like the CDI and EDD to estimate taxable income, where an appellant has
5 failed to file his own return, is reasonable and rational. (See Rev. & Tax. Code, § 18648; *Appeals of*
6 *Walter R. Bailey*, 92-SBE-001, Feb. 20, 1992; *Appeals of R. and Sonja J. Tonsberg*, 85-SBE-034,
7 Apr. 9, 1985.)

8 Once respondent has met its burden, the assessment is presumed correct and the appellant
9 has the burden of proving it to be wrong. (*Todd v. McColgan, supra; Appeal of Michael E. Myers,*
10 *supra.*) Unsupported assertions are not sufficient to satisfy appellant's burden of proof. (*Appeal of*
11 *Aaron and Eloise Magidow*, 82-SBE-274, Nov. 17, 1982.) In the absence of uncontradicted, credible,
12 competent, and relevant evidence showing error in respondent's determinations, they must be upheld.
13 (*Appeal of Oscar D. and Agatha E. Seltzer*, 80-SBE-154, Nov. 18, 1980.) An appellant's failure to
14 produce evidence that is within his control gives rise to a presumption that such evidence is unfavorable
15 to his case. (*Appeal of Don A. Cookston*, 83-SBE-048, Jan. 3, 1983.)

16 The Board has previously considered and rejected each of appellant's contentions as
17 frivolous and without merit. (See *Appeals of Robert E. Wesley, et al.*, 2005-SBE-002, Nov. 15, 2005;
18 *Appeal of Michael E. Myers, supra; Appeal of Alfons Castillo*, 92-SBE-020, July 20, 1992; *Appeal of*
19 *Walter R. Bailey, supra; and Appeals of Fred R. Dauberger, et al.*, 82-SBE-082, Mar. 31, 1982.)

20 California imposes a penalty for the failure to file a return on or before the due date,
21 unless it is shown that the failure is due to reasonable cause and not due to willful neglect. (Rev. & Tax.
22 Code, § 19131.) To establish reasonable cause, the taxpayer "must show that the failure to file timely
23 returns occurred despite the exercise of ordinary business care and prudence, or that cause existed as
24 would prompt an ordinary intelligent and prudent businessman to have so acted under similar
25 circumstances." (*Appeal of Howard G. and Mary Tons*, 79-SBE-027, Jan. 9, 1979.)

26 Finally, the Board may impose a penalty of up to \$5,000 whenever it appears to the
27 Board that proceedings before it have been instituted or maintained primarily for delay or that the
28 position is frivolous or groundless. (Rev. & Tax. Code, § 19714.) Appellant was notified of this fact in

1 the NOA's dated May 11, 2005, and in letters from Board staff dated July 3, 2009. The following non-
2 exclusive list of factors is considered in determining whether, and in what amount, to impose a frivolous
3 appeal penalty:

- 4 (1) Whether appellant is making arguments that the Board, in a Formal Opinion, or
5 courts have rejected;
- 6 (2) Whether appellant is making the same arguments that the same appellant made in
7 prior appeals;
- 8 (3) Whether the appellant filed the appeal with the intent of delaying legitimate tax
9 proceedings or the legitimate collection of tax owed;
- 10 (4) Whether the appellant has a history of filing frivolous appeals or failing to comply
11 with California's tax laws. (Cal. Code Regs., tit. 18, § 5454, subd. (b).)

12 Staff Comments

13 Respondent based its assessment on information from the CDI. The Board previously
14 concluded that methods of estimating income like this are rational and reasonable, and, thus, the burden
15 of proof has shifted to appellant in this matter. In this case, the shift in the burden does not require
16 appellant to prove error on the part of the FTB, but merely to produce evidence (which should be in his
17 possession) of his actual income. Appellant, therefore, should provide evidence to substantiate his
18 contentions and rebut the assessment made by respondent, as well to substantiate reasonable cause for
19 relief from the penalties.

20 Respondent states that appellant has not filed a tax return since 1995. Respondent issued
21 filing enforcement proposed assessments for tax years 2001 through 2007. The assessments for 2002,
22 2003, and 2005 are final assessments, due and payable. Respondent has issued NPA's for 2006 and
23 2007, which appellant has protested.⁵ This appeal consolidates appellant's appeals for 2001 and 2004.
24 The Board has not imposed a Frivolous Appeal Penalty for this appellant prior to this consolidated
25 appeal.

26 The Board's final decision should account for respondent's concession of the \$671.50
27 demand penalty for 2001.

28 ///

Sykes_jj

⁵ Appellant has appealed the assessment for 2006 to the Board (Case No. 512493). As of the writing of this summary, the briefing has not been completed on this appeal.