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10 **BOARD OF EQUALIZATION**

11 **STATE OF CALIFORNIA**

12 In the Matter of the Appeal of:) **HEARING SUMMARY²**
13) **PERSONAL INCOME TAX APPEAL**
14 **VINCENT J. MARANTO AND**) Case No. 612999
15 **SUSAN L. MARANTO¹**)

| Year | Proposed Assessment | |
|------|---------------------|------------------------|
| | Tax | Penalties ³ |
| 1998 | \$ 285.00 | \$ 193.72 |
| 1999 | \$ 11,259.00 | \$ 5,425.62 |
| 2000 | \$ 9,971.00 | \$ 1,344.97 |

16 Representing the Parties:

17 For Appellants: James G. LeBloch, Attorney
18 For Franchise Tax Board: Jean M. Cramer, Tax Counsel IV

19 ¹ Appellants reside in Orange County.

20 ² This matter was originally scheduled for oral hearing at the Board's April 24-25, 2013 Culver City Board meeting, but was postponed to allow appellant's representative additional time to prepare for the hearing. This matter was rescheduled for the Board's July 17-18, 2013 Culver City Board meeting.

21 ³ The following penalties were assessed. For the 1998 tax year, a \$100.00 late filing penalty and a \$93.72 post-amnesty penalty were assessed. For the 1999 tax year, a \$2,766.00 late filing penalty and a \$2,659.62 post-amnesty penalty were assessed. For the 2000 tax year, a \$1,344.97 post-amnesty penalty was assessed.

22 Respondent has indicated that it will abate the \$100 late filing penalty assessed for the 1998 tax year following the close of this appeal.

1 QUESTIONS: (1) Whether the Franchise Tax Board's (respondent's or the FTB's) proposed
2 assessments for the tax years at issue are barred by the statute of limitations;
3 (2) Whether appellants established error in respondent's proposed assessments,
4 which are based on final federal determinations for the tax years at issue;
5 (3) Whether appellants have established reasonable cause for the late filing of their
6 1999 tax return to abate the late filing penalty; and
7 (4) Whether the Board has jurisdiction to review the proposed post-amnesty
8 penalties.

9 HEARING SUMMARY

10 Background

11 Appellants filed an untimely 1998 California income tax return on March 1, 2000.
12 Appellants reported a California adjusted gross income (AGI) of \$101,726, and claimed total
13 deductions of \$16,434, resulting in a taxable income of \$85,292. Appellants reported a self-assessed
14 tax of \$4,634, and exemption credits of \$646, resulting in a tax liability of \$3,988 (i.e., \$4,634 - \$646).
15 Because appellants' withholding credits and excess California SDI credits totaled \$4,780, respondent
16 transferred the overpayment of \$792 (i.e., \$4,780 - \$3,988), plus accrued interest, to appellants' 1992
17 tax year. (Resp. Op. Br., p. 2, Exs. A, B, & C.)

18 Appellants filed an untimely 1999 California income tax return on April 15, 2001.
19 Appellants reported a California AGI of \$127,918 and claimed total deductions of \$30,708, resulting
20 in a taxable income of \$97,210. Appellants reported a self-assessed tax of \$5,656, and exemption
21 credits of \$598, resulting in a tax liability of \$5,058. Because appellants' withholding credits and
22 excess California SDI credits totaled \$4,853, appellants had a balance due of \$205 (i.e., \$5,058 -
23 \$4,853), which they remitted with their return. Respondent imposed a \$100 late filing penalty, plus
24 accrued interest, that appellants paid in full on May 8, 2001. (Resp. Op. Br., p. 2, Exs. D, E, & F.)

25 Appellants filed a California income tax return for the 2000 tax year on or before
26 April 15, 2001. Appellants reported a California AGI of \$127,438 and claimed total deductions of
27 \$30,983, resulting in a taxable income of \$96,455. Appellants reported a self-assessed tax of \$5,466 and
28 exemption credits of \$620, resulting in a tax liability of \$4,846. Because appellants' withholding credits

1 totaled \$3,655, appellants had a balance due of \$1,191 (i.e., \$4,846 - \$3,655), which they remitted with
2 their return. (Resp. Op. Br., p. 2, Exs. G, H, & I.)

3 The Internal Revenue Service (IRS) audited appellants' 1998, 1999, and 2000 federal tax
4 returns and made adjustments to appellants' income and itemized deductions, which increased
5 appellants' taxable income for all three years. Respondent was not notified by appellants of the federal
6 adjustments or of the final federal determinations. It appears that, on October 15, 2010, respondent
7 received Revenue Agent's Reports (RARs) from the IRS detailing the federal adjustments made to
8 appellants' 1998, 1999, and 2000 tax years. Based on this information, respondent issued Notices of
9 Proposed Assessment (NPAs) for all three tax years on July 27, 2011. The NPAs followed the federal
10 adjustments as shown on the RARs and the deficiency assessments posted on appellants' federal account
11 transcripts. (Resp. Op. Br., p. 2, Exs. J, K, L, M, N, O, & P.)

12 For the 1998 tax year, respondent issued an NPA proposing to increase appellants'
13 taxable income by \$3,060, which included \$3,000 for a capital gain and \$60 in disallowed itemized
14 deductions, for a revised taxable income of \$88,352 (i.e., \$85,292 + \$3,060). Based on these
15 adjustments, respondent increased appellants' California tax liability by \$285 (i.e., \$4,272 - \$3,988).
16 Respondent also imposed a \$100.00 late filing penalty⁴ and a \$93.72 post-amnesty penalty, plus interest.
17 (Resp. Op. Br., p. 2, Ex. K.)

18 For the 1999 tax year, respondent issued an NPA proposing to increase appellants'
19 taxable income by \$121,055, which included the \$1,200 for unreported income from South Coast
20 Insurance Marketing, \$100,000 in gain from the sale of Maranto Enterprises, Inc., \$19,871 in disallowed
21 itemized deductions, and a reduction of \$16 for the self-employment tax, for a revised taxable income of
22 \$218,265 (i.e., \$97,210 + \$121,055). Based on these adjustments, respondent increased appellants'
23 California tax liability by \$11,259 (i.e., \$16,317 - \$5,058). Respondent also imposed a \$2,766.00 late
24 filing penalty and a \$2,659.62 post-amnesty penalty, plus accrued interest. (Resp. Op. Br., pp. 2-3, Ex.
25 L.)

26 For the 2000 tax year, respondent issued an NPA proposing to increase appellants'
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⁴ Respondent has indicated that the \$100 late filing penalty will be abated at the close of this appeal because appellants' original withholding credits were greater than their revised total tax liability. (Resp. Op. Br., p. 6.)

1 taxable income by \$107,260, which included a \$100,000 gain from the sale of Maranto Enterprises, Inc.
2 and \$7,260 in disallowed itemized deductions, for a revised taxable income of \$203,715 (i.e., \$96,455 +
3 \$107,260). Based on these adjustments, respondent increased appellants' California tax liability by
4 \$9,971 (i.e., \$14,817 - \$4,846). Respondent also imposed a \$1,344.97 post-amnesty penalty. (Resp. Op.
5 Br., p. 3, Ex. M.)

6 On September 23, 2011, respondent received appellants' protest for the tax years at issue.
7 Appellants asserted that the NPAs were barred by the statute of limitations and that the federal
8 adjustments were erroneous. Appellants contended that the returns were correct as filed, they intended
9 to provide the necessary financial data, and they were prepared to discuss the proper tax consequences.
10 (Resp. Op. Br., p. 3, Ex. Q.)

11 On January 11, 2012, respondent acknowledged appellants' protest in a letter and
12 explained the statute of limitations for deficiency assessments based on federal adjustments.
13 Respondent stated that, because appellants never notified respondent of the federal adjustments and the
14 IRS did not notify respondent of the federal adjustments until October 15, 2010, the July 27, 2011 NPAs
15 were timely within the applicable statute of limitations. Respondent also sent this letter to appellants'
16 representative. (Resp. Op. Br., p. 3, Exs. R & S.)

17 On May 14, 2012, respondent affirmed the NPAs and issued Notices of Action (NOAs)
18 for the 1998, 1999, and 2000 tax years. (Resp. Op. Br., p. 3, Ex. T, U, & V.) This timely appeal then
19 followed.

20 Contentions

21 Appellants' Appeal Letter

22 On appeal, appellants make the same contentions as in their protest letter. Appellants
23 contend that the proposed assessments are barred by the statute of limitations. Appellants assert that all
24 assessments must be made within three years of the date that the returns were filed. Appellants also
25 contend that the federal adjustments are based on erroneous additions to income and erroneous
26 reductions in allowable deductions and the returns were correct as filed. Appellants state that they
27 intend to provide the necessary financial data and are prepared to discuss the proper tax consequences.
28 (Appeal Letter, pp. 1-2.)

1 Respondent's Opening Brief

2 Respondent contends that the July 27, 2011 NPAs were issued timely. Respondent
3 contends that, pursuant to R&TC sections 19059 and 19060, a proposed assessment based on changes or
4 corrections at the federal level is one of the express exceptions to the general four-year statute of
5 limitations for proposed deficiency assessments. Respondent contends that R&TC section 18622
6 requires appellants to report federal changes to respondent within six months of the final federal
7 determination of the federal changes. Respondent contends that, according to R&TC section 19059, if
8 the federal determination is reported to respondent within this six-month time period, respondent must
9 issue a notice of proposed deficiency within two years of the date that the federal action is reported to
10 respondent. Respondent further contends that, according to R&TC section 19060, subdivision (b), if the
11 federal determination is reported after the six-month period, respondent must issue a notice of proposed
12 deficiency within four years of the date that the federal action is reported to respondent. Respondent
13 notes that the final federal determination date is the date on which each federal adjustment is "assessed"
14 to the federal account by the IRS, citing R&TC section 18622, subdivision (d), and Internal Revenue
15 Code (IRC) section 6203. Respondent notes that the final federal determination date for appellants'
16 1998 tax year was December 13, 2004, and for appellants' 1999 and 2000 tax years was May 22, 2006.
17 As such, respondent contends that appellants were required to report the federal changes to respondent
18 within six months of those dates, or by June 13, 2005 and November 22, 2006. Respondent contends
19 that as appellants failed to report the federal changes to respondent and the IRS did not report the federal
20 changes until October 15, 2010, respondent had until October 15, 2014 to mail NPAs for appellants'
21 1998, 1999, and 2000 tax years based on those federal changes. (Resp. Op. Br., pp. 3-4, Exs. X, Y, &
22 Z.)

23 Respondent also contends that appellants failed to demonstrate error in the proposed
24 assessments based on the federal adjustments. Respondent contends that, when the IRS makes changes
25 or corrections to a taxpayer's tax return, the taxpayer must either concede the accuracy of the federal
26 determination or prove the federal changes are erroneous, citing R&TC section 18622, subdivision (a).
27 Respondent notes that its review of recently-obtained federal individual account transcripts for the 1998,
28 1999, and 2000 tax years show no change or abatement of the federal deficiency assessments.

1 Respondent further notes that the federal transcripts show that appellants agreed to the assessments for
2 their 1999 and 2000 tax years and signed a document to that effect on March 31, 2006. Respondent
3 contends that appellants have not provided any information to prove that the federal adjustments were in
4 error. Without evidence to support their claims, respondent contends that appellants failed to establish
5 that the federal actions, and the proposed assessments based thereon, were in error. (Resp. Op. Br., p. 5,
6 Exs. X, Y, & Z.)

7 Respondent further contends that the remaining late filing penalty was properly imposed
8 and appellants have not demonstrated reasonable cause to abate the late filing penalty for the 1999 tax
9 year. Respondent notes that the 1999 tax return was filed on April 15, 2001. Respondent contends that
10 this return was filed well past the original due date of April 15, 2000. Respondent contends that, as
11 appellants have not made any specific arguments as to why the return was untimely and failed to provide
12 any evidence demonstrating that reasonable cause, and not willful neglect, caused the late filing,
13 appellants failed to carry their burden of proof and the penalty should not be abated. With regard to the
14 post-amnesty penalty, respondent contends that the Board does not currently have jurisdiction to
15 consider respondent's imposition of the penalty. Respondent contends that, pursuant to R&TC section
16 19777.5, subdivisions (e)(1) and (2), the Board's jurisdiction is limited to when the post-amnesty
17 penalty is assessed as a final liability and has been paid and the taxpayer files a refund claim on the
18 grounds that the amount paid to satisfy the penalty was not properly computed by the FTB. (Resp. Op.
19 Br., pp. 5-7.)

20 Appellants' Reply Brief

21 Appellants contend that the federal adjustments are erroneous because they received a
22 stipulated decision in settlement as a result of challenging the federal assessment in the United States
23 Tax Court (Tax Court). Appellants provide the docket sheet for their Tax Court case which indicates
24 that appellants agreed to a stipulated decision that was affirmed by the Tax Court on March 31, 2006.
25 (App. Reply Br., p. 1.)

26 Respondent's Reply Brief

27 Respondent contends that appellants mistakenly contend that the proposed assessments
28 are not based on the stipulated agreement between appellants and the IRS that settled their federal audit.

1 Respondent notes that, in its opening brief, respondent indicated that the federal transcript shows
2 appellants agreed to the federal assessments for their 1999 and 2000 tax years and signed a document to
3 that effect on March 31, 2006. Respondent contends that this statement is based on appellants'
4 Individual Master Files (IMFs). Respondent further notes that appellants' IMFs indicated that the
5 federal amounts assessed are the same as the amounts indicated on the RARs. As such, respondent
6 contends that the federal adjustments it relied on in its proposed assessment are the same federal
7 adjustments which appellants agreed to and are correct. Respondent contends that the entry of a
8 stipulated decision on the Tax Court docket dated March 31, 2006, directly correlates with the IRS
9 actions entered on the 1999 and 2000 IMFs and shows that respondent relied on the correct federal
10 information for the proposed assessments for appellants' 1998, 1999, and 2000 tax years.⁵

11 (Resp. Reply Br., pp. 1-3.)

12 Applicable Law

13 Statute of Limitations – Deficiency Assessment

14 R&TC section 19057, subdivision (a), provides generally that every NPA shall be mailed
15 to the taxpayer within four years after the return was filed. R&TC section 18622, subdivision (a),
16 provides, in pertinent part, that if any item required to be shown on a federal tax return for any year for
17 any taxpayer is changed or corrected by the IRS, that taxpayer shall report each change or correction
18 within six months after the final federal determination of the change or correction and concede the
19 accuracy of the determination or state why it is erroneous. If a taxpayer notifies respondent of the
20 federal changes or corrections within six months of the final federal determination, then respondent has
21 the later of the two years from the date of the taxpayer's notice or the general four year statute of
22 limitations pursuant to R&TC section 19057 to issue a proposed assessment based on the federal
23 adjustments. (Rev. & Tax. Code, § 19059.) If, after the six-month period required by R&TC section
24 18622, the taxpayer or the IRS reports a change or correction by the IRS, a notice of deficiency may be
25 mailed to the taxpayer within four years from the date that the taxpayer or the IRS notifies respondent of
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28 ⁵ However, respondent notes that the docket entries do not indicate whether appellants included the 1998 tax year in their petition to the Tax Court. Respondent notes that the IMF does not list any abatement of the prior tax assessed nor have appellants submitted any evidence of a revision or a revocation of the 1998 deficiency assessment.

1 that change or correction. (Rev. & Tax. Code, § 19060, subd. (b).) Finally, if the taxpayer fails to notify
2 the FTB of the federal changes, then the FTB may issue the notice of deficiency at any time. (Rev. &
3 Tax. Code, § 19060, subd. (a); *Ordlock v. Franchise Tax Board* (2006) 38 Cal.4th 897.) A final
4 determination is an irrevocable determination or adjustments of a taxpayer's federal tax liability from
5 which there exists no further right of either an administrative or judicial appeal. (Cal. Code of Regs.,
6 tit. 18, § 19059, subd. (e).)

7 Accuracy of Assessment Based on Federal Adjustments

8 R&TC section 18622, subdivision (a), provides that taxpayers shall either concede the
9 accuracy of a federal determination or state wherein it is erroneous. It is well-settled that a deficiency
10 assessment based on a federal audit report is presumptively correct and the appellants bear the burden of
11 proving that the determination is erroneous. (*Appeal of Sheldon I. and Helen E. Brockett*, 86-SBE-109,
12 June 18, 1986; *Todd v. McColgan* (1949) 89 Cal.App.2d 509.) Unsupported assertions are not sufficient
13 to satisfy the appellants' burden of proof with respect to an assessment based on federal action. (*Appeal*
14 *of Aaron and Eloise Magidow*, 82-SBE-274, Nov. 17, 1982.) The appellants' failure to produce
15 evidence that is within their control gives rise to a presumption that such evidence is unfavorable to their
16 case. (*Appeal of Don A. Cookston*, 83-SBE-048, Jan. 3, 1983.)

17 Deductions from gross income are a matter of legislative grace and the taxpayers have the
18 burden of proving an entitlement to the deductions claimed; unsupported assertions are not sufficient to
19 satisfy the taxpayers' burden of proof. (*New Colonial Ice Co. v. Helvering* (1934) 292 U.S. 435; *Appeal*
20 *of James C. and Monablance A. Walshe*, 75-SBE-073, Oct. 20, 1975.) To carry the burden of proof,
21 the taxpayers must point to an applicable statute and show by credible evidence that the deductions
22 claimed come within its terms. (*Appeal of Robert R. Telles*, 86-SBE-061, Mar. 4, 1986.) In the absence
23 of uncontradicted, credible, competent, and relevant evidence showing that respondent's determinations
24 are incorrect, such assessments must be upheld. (*Appeal of Oscar D. and Agatha E. Seltzer*, 80-SBE-
25 154, Nov. 18, 1980.)

26 Late Filing Penalty

27 R&TC section 19131 provides that a late filing penalty shall be imposed when a taxpayer
28 fails to file a tax return on or before its due date, unless the taxpayer establishes that the late filing was

1 due to reasonable cause and was not due to willful neglect. The penalty is specified as 5 percent of the
2 tax due for each month that a valid tax return is not filed after it is due, not to exceed 25 percent of the
3 tax. (Rev. & Tax. Code, § 19131, subd. (a).) To establish reasonable cause, a taxpayer “must show that
4 the failure to file timely returns occurred despite the exercise of ordinary business care and prudence, or
5 that cause existed as would prompt an ordinary intelligent and prudent businessman to have so acted
6 under similar circumstances.” (*Appeal of Howard G. and Mary Tons*, 79-SBE-027, Jan. 9, 1979.)

7 Post-Amnesty Penalty

8 In 2004, the Legislature enacted Senate Bill 1100 which authorized respondent to institute
9 an income tax amnesty program. (Rev. & Tax. Code, §§ 19730-19738.) Under R&TC section 19777.5,
10 there are essentially two amnesty penalties: one for unpaid liabilities that existed at the time of amnesty,
11 and a second post-amnesty penalty based on subsequent assessments, including self-assessments. (Rev.
12 & Tax. Code, § 19777.5, subds. (a)(1) and (a)(2).) As relevant to this appeal, the post-amnesty penalty is
13 calculated as the amount equal to 50 percent of the interest computed under R&TC section 19101 on the
14 tax underpayment for the period beginning on the last date prescribed by law for the payment of tax and
15 ending on March 31, 2005. (Rev. & Tax. Code, § 19777.5, subd. (a)(2).)

16 The Board’s jurisdiction to review an amnesty penalty is extremely limited. For
17 example, taxpayers have no right to an administrative protest or appeal of an unpaid amnesty penalty.
18 (Rev. & Tax. Code, § 19777.5, subd. (d).) Taxpayers also have no right to file an administrative claim
19 for refund of a paid amnesty penalty, except upon the basis that the penalty was not properly computed.
20 (*Id.* subd. (e).) Therefore, the Board’s jurisdiction to review an amnesty penalty is limited to situations
21 where the penalty is assessed and paid, the taxpayers file a timely appeal from a denial of a refund
22 claim, and the taxpayers attempt to show a computational error in the penalty.

23 STAFF COMMENTS

24 Statute of Limitations

25 Appellants did not notify respondent of the federal adjustments or the final federal
26 determinations for the 1998, 1999, and 2000 tax years. Respondent did not receive notification of the
27 federal adjustments until the IRS provided respondent with the RARs on October 15, 2010. In
28 accordance with R&TC section 19060, subdivision (b), respondent had until four years from that date, or

1 until October 15, 2014, to issue the NPAs. As the NPAs here were issued on July 27, 2011, it appears
2 that the proposed assessments are timely.

3 Federal Adjustments

4 Appellants contend that the federal adjustments are erroneous because they received a
5 stipulated decision in a settlement as a result of challenging the federal assessment in the Tax Court. It
6 appears to staff that respondent's proposed assessments are based on federal adjustments as reflected in
7 appellants' IMFs and are correct. According to the IMFs, appellants agreed to the assessments for the
8 1999 and 2000 tax years and signed an agreement on March 31, 2006, which corresponds to the date
9 appellants received the stipulated decision from the Tax Court. Prior to the hearing, appellants should
10 provide a copy of the March 31, 2006 stipulated decision, and they should be prepared to discuss its
11 contents at the hearing.

12 Appellants also indicate that they had evidence to support the positions taken on their tax
13 returns. However, appellants have yet to provide any such information to respondent or the Board. If
14 either party has any additional evidence to present, they should provide their evidence to the Board
15 Proceedings Division at least 14 days prior to the oral hearing pursuant to California Code of
16 Regulations, title 18, section 5523.6.⁶

17 Late Filing Penalty

18 Appellants have not alleged nor provided evidence of reasonable cause and not willful
19 neglect caused the untimely filing of the 1999 tax return.

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28 ⁶ Evidence exhibits should be sent to: Claudia Madrigal, Staff Services Manager, Board Proceedings Division, State Board of
Equalization, P.O. Box 942879 MIC:80, Sacramento, California, 94279-0080.