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9 **BOARD OF EQUALIZATION**
10 **STATE OF CALIFORNIA**

11 In the Matter of the Appeal of:) **HEARING SUMMARY**
12) **PERSONAL INCOME TAX APPEAL**
13 **ROBERT M. NEWELL, JR. AND**) Case No. 506927
14 **JUDITH A. NEWELL**¹)

15 Year Claim
16 2007 For Refund²
17 \$3,532

18 Representing the Parties:

19 For Appellants: Robert M. Newell, Jr.
20 Judith A. Newell

21 For Franchise Tax Board: Eric A. Yadao, Administrator I

22 **QUESTION:** Whether appellants have shown the late filing penalty imposed by respondent
23 should be abated.

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26 ¹ Appellants reside in San Marino, Los Angeles County, California.

27 ² This is the amount of the late filing penalty, as reflected in respondent's information. (Resp. Opening Br., p. 1, Exhibit A,
28 p. 2.)

Robert M. Newell, Jr. and
Judith A. Newell

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1 HEARING SUMMARY

2 Background

3 Appellants submitted estimated quarterly tax payments totaling \$32,000 for tax year
4 2007, but did not file a 2007 return by the extended due date of October 15, 2008. (Resp. Opening
5 Br., p. 1.) On October 27, 2008, appellants filed their 2007 return and remitted a payment of \$14,128.
6 On their 2007 return, appellants reported a total tax liability of \$46,128. (*Ibid.*)³ Respondent accepted
7 the return as filed and issued a Return Information Notice to appellants dated November 5, 2008,
8 advising appellants that it was imposing a late filing penalty of \$3,532.00, which is 25 percent of the
9 late paid tax of \$14,128.00, and an estimated tax penalty of \$231.08, plus interest of \$716.40. (*Ibid.*;
10 Apps. Opening Br., Attachment.)

11 Mr. Newell sent respondent a letter dated November 19, 2008, in which he requested
12 abatement of the penalties and stated that his accountant will explain why abatement is appropriate.⁴
13 With his November 19, 2008, letter, Mr. Newell enclosed a check for \$716.40 in satisfaction of the
14 assessed interest. (Apps. Opening Br., Attachment.) Respondent sent appellants a Final Notice dated
15 March 17, 2009, advising appellants that it could begin collection actions without further notice if
16 appellants did not pay the balance due of \$3,843.41, which consists of tax of \$46,128.00, a penalty
17 amount of \$3,763.08 (\$3,532.00 + \$231.08) and interest of \$796.73 less payments of \$46,844.40
18 (\$32,000.00 + \$14,128.00 + \$716.40). (*Ibid.*) On or about March 19, 2009, appellants paid the
19 balance due of \$3,843.41. (*Ibid.*) In a letter to respondent dated April 27, 2009, Mr. Newell made an
20 “‘informal refund claim’ for penalties paid.” (*Ibid.*) In a letter dated May 28, 2009, respondent
21 informed appellants that their claim for refund in the amount of \$3,532 had been denied.⁵ (*Ibid.*)
22 Appellants filed this timely appeal with respect to the late filing penalty of \$3,532.

23 _____
24 ³ A copy of appellants’ 2007 return is not in the file.

25 ⁴ Staff notes that there is no correspondence from appellants’ accountant in the file.

26 ⁵ It is not clear to staff why respondent assumed in its May 28, 2009, letter that appellants’ claim for refund was limited to the
27 amount of the late filing penalty, \$3,532.00, because appellants requested a refund of “penalties paid” in their April 27, 2009,
28 letter, which might also include the paid estimated tax penalty of \$231.08.

1 Appellants' Contentions

2 In their appeal letter, appellants state that they are appealing respondent's denial of
3 their claim for refund of the late filing penalty of \$3,532.00 for tax year 2007, but are not seeking
4 relief from the paid estimated tax penalty of \$231.08. Appellants contend that there is good cause for
5 at least partial relief from penalties. In their appeal letter, appellants contend that they are entitled to
6 abatement of penalties for the reasons listed in Mr. Newell's April 27, 2009, letter to respondent and
7 because, on numerous occasions, they overpaid estimated taxes for which they received no interest or
8 other benefit. The reasons for abatement set forth in Mr. Newell's April 27, 2009, letter are as
9 follows: 1) he had a one-time substantial capital gain for tax year 2007 that accrued late in 2007,
10 which he did not anticipate in making his earlier quarterly payments; 2) he had not realized (or had
11 forgotten) that California treats capital gains as ordinary income; 3) he paid the full amount of interest
12 of \$796.73, for which he is not seeking an adjustment; and 4) he did not receive his 2007 Partnership
13 K-1 form until mid-October 2008 due to delays caused by the firm's accountants for which he had no
14 control. In his April 27, 2009, letter, Mr. Newell also states that it is reasonable and fair to request
15 abatement of penalties because he did not act in bad faith, he fully paid the accrued interest, and agrees
16 that any refund may be applied to his 2008 or 2009 tax obligations.

17 In his reply brief, Mr. Newell contends that his inability to receive his K-1 form until
18 October 2008 is reasonable cause for the abatement of the late filing penalty and it does not
19 "implicate" willful neglect. According to Mr. Newell, he and his partners are wholly dependent upon
20 their K-1 forms to file timely returns and to pay the correct amount of tax. He contends that he made
21 many requests to the firm's accounting staff about the need to get their information collected and to
22 coordinate with their outside accountant. He asserts, "Calculation of 401K contributions to our staff
23 along with establishing an appropriate formula to calculate the proper amount seem to be the main
24 choke points each year." He further asserts that his firm's partners, bookkeepers and outside
25 accountants met on several occasions in 2008 and 2009 to discuss and resolve these issues. He also
26 contends that they believe they currently have a plan beginning with the 2009 tax year that will allow
27 them to process the necessary information in a more timely manner. Mr. Newell also asserts that
28 without protest he and his wife paid "above-market" interest on the 2007 amount due, and for tax year

Robert M. Newell, Jr. and
Judith A. Newell

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1 2008, they overpaid their estimated taxes by a modest amount and they expect to do the same for tax
2 year 2009. Mr. Newell argues that it is unduly harsh for respondent to impose a 25 percent late filing
3 penalty for a return that was filed only 12 days after the extended due date of October 15, 2008.
4 Lastly, Mr. Newell requests that the Board stays the close of briefing until the Internal Revenue
5 Service (IRS) makes a final determination with respect to appellants' request for abatement of a
6 similar federal penalty; Mr. Newell provided contact information for the pertinent IRS appeals officer.

7 Respondent's Contentions

8 Respondent contends that there is a presumption that it properly imposed the late filing
9 penalty and appellants have the burden of showing that the late filing occurred due to reasonable cause
10 and not due to willful neglect. Respondent contends that ordinary care and prudence means that the
11 taxpayer's reason must be such that an ordinarily intelligent and prudent businessperson would have
12 acted similarly under the same circumstances. Respondent contends that appellants' late recognition
13 of a one-time substantial capital gain has no bearing on the late filing penalty, but rather pertains to the
14 estimated tax penalty, which they are not appealing. Respondent asserts nonetheless that appellants'
15 lack of necessary information does not establish reasonable cause to abate the late filing penalty.
16 Similarly, respondent contends that appellants' lack of awareness or recollection that California treats
17 capital gains as ordinary income pertains to the estimated tax penalty, rather than the late filing
18 penalty. Respondent argues that appellants' ignorance of the law with respect to capital gains also
19 does not establish reasonable cause to abate the late filing penalty. Respondent contends that its
20 authority to charge interest on the late payment of taxes and impose penalties for underestimated tax is
21 independent of its authority to impose a late filing penalty. Respondent therefore argues that
22 appellants' election not to appeal the interest assessed or the estimated tax penalty is not reasonable
23 cause for the abatement of the late filing penalty. Furthermore, respondent points out that appellants
24 filed late returns for tax years 2000, 2001, 2002, 2003, and 2006. (Resp. Opening Br., p. 3, Exhibit
25 D.) Respondent further points out that it imposed and waived the late filing penalty for tax year 2006,
26 but that it imposed the late filing penalty for 2001, which appellants paid. (*Id.*, Exhibit E.)

27 Respondent contends that it will follow the determination of the IRS when it consists of
28 a finding of reasonable cause for abatement of the same penalty. (Resp. Opening Br., p. 2, fn. 2.)

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1 According to respondent, appellants' IRS Individual Master File (IMF) shows that the IRS imposed a
2 late filing penalty for tax year 2007, but did not abate the penalty. (*Ibid.*, Exhibit C.) Respondent
3 asserts that there is no alternative federal basis for it to abate appellants' late filing penalty. (*Ibid.*)

4 Applicable Law

5 Individuals must file California income tax returns on or before April 15, or on or
6 before the extended due date of October 15, following the tax year. (Rev. & Tax. Code, §§ 18566,
7 18567, subd. (a).) Revenue and Taxation Code (R&TC) section 19131 provides that a delinquent
8 filing penalty of 5 percent shall be added to the tax for each month that a return is filed late, not to
9 exceed 25 percent of the additional tax, unless the taxpayer can establish reasonable cause and no
10 willful neglect.⁶ The taxpayer bears the burden of proving that both conditions existed. (*Appeal of*
11 *Terry R. Lash*, 86-SBE-021, Feb. 4, 1986; *Appeal of Kerry and Cheryl James*, 83-SBE-009,
12 Jan. 3, 1983.) On appeal, there is a presumption of correctness of the penalties assessed by
13 respondent. (*Appeal of Robert Scott*, 83-SBE-094, Apr. 5, 1983.) To establish reasonable cause, the
14 taxpayer "must show that the failure to file timely returns occurred despite the exercise of ordinary
15 business care and prudence, or that cause existed as would prompt an ordinary intelligent and prudent
16 businessman to have so acted under similar circumstances." (*Paramount Development Associates,*
17 *Inc.*, 83-SBE-250, Dec. 14, 1983; *Appeal of Howard G. and Mary Tons*, 79-SBE-027, Jan. 9, 1979.)

18 In previous appeals, we determined that a taxpayer's discovery of reportable income after
19 the original due date (*Appeal of Elixir Industries*, 83-SBE-248, Dec. 14, 1983), a taxpayer's difficulty in
20 obtaining necessary information (*Appeal of J.B. and P.R. Campbell*, 85-SBE-112, Oct. 9, 1985; *Appeal*
21 *of Stephen C. Bieneman*, 82-SBE-148, July 26, 1982; *Appeal of William T. and Joy P. Orr*, 68-SBE-010,
22 Feb. 5, 1968), a taxpayer's difficulty in resolving accounting problems (*Appeal of Cerwin-Vega*
23 *International*, 78-SBE-070, Aug. 15, 1978), a taxpayer's difficulty in determining income with
24 exactitude (*Appeal of Roger W. Sleight*, 83-SBE-244, Oct. 26, 1983; *Appeal of Avco Financial Services,*
25

26 ⁶ The United States Supreme Court defined willful neglect as a "conscious, intentional failure or reckless indifference."
27 (*United States v. Boyle* (1985) 469 U.S. 241, 245-246.) Respondent does not appear to allege the existence of willful neglect
28 on the part of appellant.

1 *Inc.*, 79-SBE-084, May 9, 1979), a taxpayer's unresolved business matters (*Appeal of Bild Industries,*
2 *Inc.*, 82-SBE-212, Sept. 21, 1982), or the failure of the taxpayer's accountant to properly account for
3 income (*Appeal of M.B. and G.M. Scott*, 82-SBE-249, Oct. 14, 1982) did not constitute reasonable cause
4 for abating penalties.

5 In *Appeal of M.B. and G.M. Scott, supra*, one of the Board's grounds for holding that the
6 taxpayers there did not have reasonable cause for late payment of tax was that they had access to
7 partnership information that would have allowed them to compute their tax liability well before the due
8 date of the tax. The Board in *Appeal of Roger W. Sleight, supra*, concluded that the taxpayer had not
9 shown reasonable cause for late payment of tax because all of the events necessary to compute tax on a
10 transaction occurred by October of the taxable year and the taxpayer provided no evidence why tax on
11 the transaction could not have been computed before April 15, rather than September, of the next taxable
12 year. In *Appeal of Stephen C. Bieneman, supra*, the Board held that the taxpayer there had not shown he
13 had reasonable cause for failure to file upon notice and demand because, although he alleged that he had
14 made diligent but unsuccessful efforts to obtain relevant partnership records located in other states, it did
15 not know the extent or nature of his efforts.

16 STAFF COMMENTS

17 The parties should be prepared to discuss at the oral hearing whether reasonable cause for
18 relief from the late filing penalty exists. Appellants should specifically be prepared to discuss precisely
19 the extent and nature of their purported diligent efforts to obtain the necessary partnership information
20 *prior* to the filing deadline in order to establish that they used ordinary business care and prudence.
21 Staff notes that the Board's previous holdings indicate the importance of preparing and filing a timely
22 tax return and timely paying the tax due, even in the face of business difficulties or difficulties in
23 obtaining necessary information.

24 Respondent should confirm at the oral hearing whether the IRS has already reviewed the
25 federal late filing penalty imposed for tax year 2007 and determined not to abate it. Appellants should
26 clarify at the oral hearing whether they requested from the IRS abatement of the federal late filing
27 penalty imposed for tax year 2007 subsequent to November 24, 2008, the date that the IRS apparently
28 imposed it; in this regard, with respect to whether appellants have a pending request with the IRS to

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1 abate the federal late filing penalty, appellants should provide to the Board and respondent at least 14
2 days prior to the hearing evidence that substantiates that they requested abatement of the federal late
3 filing penalty for tax year 2007 subsequent to November 28, 2008, and provide the IRS response
4 thereto.⁷

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8 Newell>If

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28 ⁷ Exhibits should be submitted to: Claudia Madrigal, Board of Equalization, Board Proceedings Division, P. O. Box 942879 MIC: 80, Sacramento, CA 94279-0080.

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