

CALIFORNIA FRANCHISE TAX BOARD

Legal Ruling No. 105

December 15, 1953

DELINQUENCY PENALTY: FAILURE TO FILE: REASONABLE CAUSE

Syllabus:

When there is sufficient uncertainty in the law as to the taxability of the income in question, such uncertainty is reasonable cause for the failure to file and penalties will be waived.

In this case a dispute arose as to whether certain oil royalty income from oil produced in California is taxable to a nonresident. After correspondence between taxpayer and this department, the requested returns were filed accompanied by refund claims and remittance of the tax plus interest. It is argued that delinquency penalties could not be assessed as the reason for the late filing was that the law was uncertain as to the taxability of such income to a nonresident. Advice is requested whether the delay in filing was due to reasonable cause so as to justify the waiver of penalties.

Penalty for failure to file is not assessable if it is shown that the failure was due to "reasonable cause" and not due to willful neglect. No question of willful neglect is indicated in the present case. The law affixes no standard as to what will constitute "reasonable cause" for this purpose. Nor is there any rigid rule of thumb which can be applied to all cases. The courts have ruled that reasonable cause means nothing more than the exercise of ordinary business care and prudence; that the mere failure to comply with provisions of revenue laws is not a per se "without reasonable cause" violation; that it is well settled that in the application of penalties, all questions of doubt must be resolved in favor of those from whom the penalty is sought; that it is not the purpose of the law to penalize frank differences of opinion or innocent errors made despite the exercise of reasonable care.

Of course, if the law is clear as to filing requirements in a particular instance, mere ignorance of the law would not constitute reasonable cause, i.e., it would not be the exercise of "ordinary business care and prudence." On the other hand, a reasonable cause excusing the failure to file a return may exist where the belief that no return was required is based on adequate grounds. Misunderstanding due to reasonable doubt as to whether a return is required in view of conflicting rulings or decisions, or ambiguities in the law may be an acceptable excuse.

In the instant case the state of the law was such that it was probable a reasonable doubt existed in the mind of the taxpayer as to the taxability of the item; that with the uncertainties in the law and the fact that taxpayer's royalty interest with relation to the producing property itself were indirect only, the question of taxability was debatable in good faith. Consequently, the taxpayer did have reasonable cause for his failure to file on time.