

LAW SUMMARY

LATE PAYMENT OF TAX PENALTY REASONABLE CAUSE ABATEMENT

The law provides that the Franchise Tax Board (FTB) shall impose a penalty for late payment of tax when a taxpayer fails to pay the amount shown as tax on the return on or before the due date of the return, unless the taxpayer establishes that the late payment was due to reasonable cause and was not due to willful neglect. (Revenue and Taxation Code section 19132.)

1. The Burden of Proof is on the Taxpayer to Establish Reasonable Cause For Abatement of The Penalty

When the FTB imposes a penalty for late payment of tax, the law presumes that the penalty was imposed correctly. (*Todd v. McColgan* (1949) 89 Cal.App.2d 509, 201 P.2d 414; *Appeal of J.B. and P.R. Campbell*, 85-SBE-112, October 9, 1985.)

The burden of proof is on the taxpayer to show that reasonable cause exists to support abatement of the late payment penalty. (*Appeal of M.B. and G.M. Scott*, 82-SBE-249, October 14, 1982; *Appeal of Roger W. Sleight*, 83-SBE-244, October 26, 1983.)

To establish reasonable cause, a taxpayer must show that the failure to timely pay the amount shown as tax on the return occurred despite the exercise of ordinary business care and prudence. (*Appeal of M.B. and G.M. Scott*, 82-SBE-249, October 14, 1982; *Appeal of Roger W. Sleight*, 83-SBE-244, October 26, 1983.)

The taxpayer's reason for failing to pay the amount of tax shown on the return by the due date must be such that an ordinarily intelligent and prudent businessperson would have acted similarly under the circumstances. (*Appeal of Robert T. and M.R. Curry*, 86-SBE-048, March 4, 1986; *Appeal of M.B. and G.M. Scott*, 82-SBE-249, October 14, 1982.)

2. An Extension to File a Return is Not an Extension to Pay the Tax

An extension of time to file a return is not an extension of the time for payment of the tax

required to be paid on or before the original due date of the return. (Revenue and Taxation Code section 18567; *Appeal of M.B. and G.M. Scott*, 82-SBE-249, October 14, 1982; *Appeal of Roger W. Sleight*, 83-SBE-244, October 26, 1983.)

3. Difficulty in Obtaining Information or Documents Needed to Timely Pay the Tax Shown on the Return

A taxpayer's inability to pay the amount of tax shown on the return by the due date because of lack of necessary information or documents, is not considered reasonable cause. (*Appeal of M.B. and G.M. Scott*, 82-SBE-249, October 14, 1982; *Appeal of Roger W. Sleight*, 83-SBE-244, October 26, 1983.) The fact that tax information is lost, lacking, inaccurate, or difficult to obtain is insufficient to meet the taxpayer's burden of establishing reasonable cause. (*Appeal of M.B. and G.M. Scott*, 82-SBE-249, October 14, 1982; *Appeal of Roger W. Sleight*, 83-SBE-244, October 26, 1983.)

A taxpayer's difficulty in determining income with exactitude does not negate the requirement that taxpayers make payments of tax based upon a reasonably accurate estimate of their tax liability. (*Appeal of M.B. and G.M. Scott*, 82-SBE-249, October 14, 1982; *Appeal of Roger W. Sleight*, 83-SBE-244, October 26, 1983.) Further, complexity and problems in accumulating the necessary information and/or documents to complete a return is not reasonable cause for the failure to pay the tax that is due. (*Appeal of J.B. and P.R. Campbell*, 85-SBE-112, October 9, 1985.)

4. Complexity of the Tax Law

Complexity of the tax law which leads to a delay in computing tax liability, and therefore a delay in paying the tax shown on the return by the due date, is not reasonable cause. (*Appeal of Philip C. and Anne Berolzheimer*, 86-SBE-172, November 19, 1986; *Appeal of Roger W. Sleight*, 83-SBE-244, October 26, 1983.)

However, if a taxpayer relies on improper substantive advice of an accountant or tax

attorney as to a matter of tax law, such as whether the taxpayer has a tax liability, failing to pay the tax shown on the return by the due date **may** be considered reasonable cause if certain conditions are met. (*United States v. Boyle* (1985) 469 U.S. 241, 83 L.Ed.2d 622.) These conditions include: (1) the person reasonably relied on by the taxpayer is a tax professional with competency in the subject tax law, and (2) the tax professional's advice is based on the taxpayer's full disclosure of the relevant facts and documents.

5. Taxpayer Has the Burden to Show That a Timely Payment of the Tax Shown on the Return Was Made

The taxpayer bears the burden of proof on a claim that a timely payment of the tax shown on the return was made. (*Appeal of Thomas T. Crittenden*, 74-SBE-043, October 7, 1974; *Appeal of La Salle Hotel Co.*, 66-SBE-071, November 23, 1966.)

6. Financial Inability to Pay the Tax

Inability to pay the tax shown on the return by the due date because of financial circumstances may be considered reasonable cause in some cases. The determination of whether a taxpayer has demonstrated grounds for the abatement of a late payment penalty based on financial inability to pay is factually intensive and done on a case by case basis. The burden of proof to show that the penalty should be abated is on the taxpayer.

Federal Regulations related to the federal failure to pay tax penalty (Internal Revenue Code section 6651) are instructive. "A failure to pay will be considered to be due to reasonable cause to the extent that the taxpayer has made a satisfactory showing that he exercised ordinary business care and prudence in providing for payment of his tax liability and was nevertheless either unable to pay the tax or would suffer an undue hardship ... if he paid on the due date. (Treas. Reg. section 301.6651-1(c)(1).) An "undue hardship" is defined in the federal regulations as, " ... more than an inconvenience to the taxpayer. It must appear that substantial financial loss, for example, loss due to the sale of property at a sacrifice price, will result to the taxpayer ... If a market exists, the sale of property at the current market price is not ordinarily considered as resulting in an undue hardship." (Treas. Reg. section 1.6161-1(b).)

The federal regulations provide that to determine the evidentiary grounds for a finding of reasonable cause, "Consideration will be given to all the facts and circumstances of the taxpayer's financial situation, including the amount and nature of the taxpayer's expenditures in light of the income (or other amounts) he could, at the time of such expenditures, reasonably expect to receive prior to the date prescribed for the payment of the tax." (Treas. Reg. section 301.6651-1(c)(1).)

For example, a taxpayer who invests funds in speculative or illiquid assets has not exercised ordinary business care and prudence in providing for the payment of a tax liability unless, at the time of the investment, the remainder of the taxpayer's assets and estimated income will be sufficient to pay the tax or it can be reasonably foreseen that the speculative or illiquid investment made by the taxpayer can be utilized (by sale or as security for a loan) to realize sufficient funds to satisfy the tax liability. A taxpayer will be considered to have exercised ordinary business care and prudence if the taxpayer made reasonable efforts to conserve sufficient assets in a marketable form to satisfy a tax liability and nevertheless was unable to pay all or a portion of the tax when it became due. (Treas. Reg. section 301.6651-1(c)(1).)

7. Computation of Late Payment of Tax Penalty

The late payment of tax penalty is computed as five percent of the total tax unpaid plus one-half of one percent for every month the payment of tax was late. (Revenue and Taxation Code section 19132.)