

TIGER STEAK, INC.	§	STATE OF ALABAMA
BIRMINGHAM I & II MGT., INC.		DEPARTMENT OF REVENUE
3591 CAHABA BEACH ROAD	§	ADMINISTRATIVE LAW DIVISION
BIRMINGHAM, AL 35242-5222,		
	§	
Taxpayers,		DOCKET NOS. INC. 05-722
	§	INC. 05-723
v.		
	§	
STATE OF ALABAMA		
DEPARTMENT OF REVENUE.	§	

FINAL ORDER

The Revenue Department assessed Tiger Steak, Inc. for penalty and interest concerning the late filing of its 2003 Form 20SC non-resident composite income tax return.

The Department also assessed Birmingham I & II Management, Inc. for interest for the year. Both corporations (“Taxpayers”) appealed to the Administrative Law Division pursuant to Code of Ala. 1975, §40-2A-7(b)(5)a. A hearing was conducted on December 14, 2005. Warren Matthews and CPA Leonard Gray represented the Taxpayers. Assistant Counsel J.R. Gaines represented the Department.

The Taxpayers do not contest the interest assessed by the Department. The issue is whether the late penalties assessed by the Department can be waived for reasonable cause.

The Taxpayer were two of several commonly owned S corporation general partners in limited partnerships that owned Outback Steakhouse restaurants in Alabama in 2003 and prior years. Other commonly owned S corporations were Alabama III Management, Inc. and Houston County Steakhouse, Inc. CPA Leonard Gray prepared and filed the necessary tax returns for all of the S corporations.

The S corporations began negotiating for the sale of the steakhouses to Outback

Steakhouse, Inc. in late 2002. The S corporations' CPA was involved in the negotiations, and thus was unable to timely file the corporations' 2002 Form 20S returns or their Form 20SC non-resident composite returns by the March 15, 2003 due date. The CPA's daughter, who is also a CPA, timely prepared and filed extensions to file the S corporations' 20S returns. She did not file an extension request concerning the Form 20SC returns because both she and her father believed, incorrectly, that the Form 20S extensions also applied to Form 20SC. The 2002 20S and 20SC returns were filed, and the tax paid, by April 15, 2003.

The Department subsequently assessed three of the S corporations, Alabama III Management, Birmingham I and II Management, and the Houston County Steakhouse, for late penalties for 2002 because the 20SC returns were not filed by the March 15, 2003 due date. Those S corporations appealed to the Administrative Law Division. A hearing was conducted on January 20, 2005. The Administrative Law Division held that the penalties should be waived for reasonable cause. The Final Order reads in part:

The Department assessed the Taxpayers for late penalties and interest because they had failed to file the 20SC returns before the March 15, 2003 due date. The Department's position is that the extensions to file the Taxpayers' 20S returns were not also extensions to file the 20SC returns. The Taxpayers appealed.

The Taxpayers' CPA and his daughter both testified at the January 20 hearing. The CPA testified that he had always filed the Taxpayers' returns before the March 15 due date, but explained that because of the negotiations concerning the sale of the restaurants, he was unable to do so concerning the 2002 returns. His daughter consequently prepared extensions to file the Taxpayers' 20S returns before the March 15 due date. She testified that she understood that filing the 20S extensions also extended the deadline for filing the 20SC returns.

A penalty assessed by the Department may be waived for reasonable cause. Section 40-2A-11(h). Rev. Proc. 97-003 addresses the waiver of penalties and specifies that reasonable cause to waive a penalty includes a non-

recurring, honest mistake, and also the reliance on the advice of a competent tax advisor.

The Department concedes that the Taxpayers have never before filed a late return or failed to timely pay the tax due. That alone is sufficient to waive the penalties as a one-time, honest mistake. It is also clear that the Taxpayers relied on the advice of their CPA and his daughter, who are competent tax advisors. They failed to file extensions to file the Form 20SC returns only because they mistakenly believed in good faith that separate extension requests for the 20SC returns were not necessary in addition to the extension requests for the 20S returns. The penalties are waived for reasonable cause. [footnote omitted]

Alabama III Management, Inc. v. State of Alabama, Inc. 04-610 (Admin. Law Div. 3/2/05) at 2 -3.

The above Final Order, which was not appealed, also included a footnote indicating that any penalties the Department may assess against the S corporations for 2003 should also be waived – “The Department has also (preliminarily) assessed the Taxpayers for late penalties for 2003 because the Taxpayers’ CPA did not learn that a separate extension to file a 20SC return was required until after he filed the Taxpayers’ 2003 returns. Although 2003 is not in issue in this case, the Taxpayers’ reliance on their CPA to properly file their 2003 returns would also constitute reasonable cause to waive those penalties.”

As indicated, the Taxpayers’ CPA was still not aware in March 2004 that an extension to file a Form 20S return was not also an extension concerning Form 20SC. Consequently, he (or his daughter) filed only a Form 20S extension request concerning the Taxpayers’ 2003 returns. Both the Form 20Ss and the Form 20SCs were subsequently filed by April 15, 2004. Despite the footnote in the 2002 Final Order that the 2003 penalties should also be waived, the Department again assessed the Taxpayers for late penalties for

not filing the 2003 Form 20SC returns by the original due date.¹ The Taxpayers again appealed.

The Department strenuously argues that the penalties should not be waived. It contends that it was the Taxpayers' duty to timely file the returns, and that their reliance on their CPA to do so does not constitute reasonable cause, citing *U.S. v. Boyle*, 105 S.Ct. 687 (1985). The Department also contends that "Taxpayer's reliance of a tax advisor is not reasonable cause." Department's Answer, at 2 – 3.

In *Boyle*, an executor of an estate relied on his attorney to timely file the estate's tax return. The attorney negligently failed to do so. The IRS subsequently assessed the executor for late penalties. The issue was whether reliance on the attorney constituted reasonable cause to waive the penalties.

The U.S. Supreme Court held that the executor's reliance on the attorney was, under the circumstances, not reasonable cause to waive the late penalties. The executor was under a legal duty to timely file the return, or ensure that the attorney timely filed the return, by the known due date. The late penalty applied because the executor failed in that duty. The negligence of the attorney was thus attributed to the executor.

In *Boyle*, the Court distinguished the situation where a taxpayer is advised, as a matter of law, that it is unnecessary to file a return.

This case is not one in which a taxpayer has relied on the erroneous advice of counsel concerning a question of law. Courts have frequently held that "reasonable cause" is established when a taxpayer shows that he reasonably relied on the advice of an accountant or attorney that it was unnecessary to

¹ Late penalties were included in the preliminary assessment entered against Tiger Steak, Inc. However, the Department apparently waived the penalties because the final assessment entered against Tiger Steak, Inc. is for interest only. There is no evidence explaining why the Department assessed one of the Taxpayers involved in this case concerning 2003, but not the other related S corporations.

file a return, even when such advice turned out to have been mistaken. (cites omitted) This Court also has implied that, in such a situation, reliance on the opinion of a tax adviser may constitute reasonable cause for failure to file a return. (cites omitted)

Boyle, 105 S.Ct. at 631.

The rationale of *Boyle* does not apply in this case because the Taxpayers' CPA understood that filing an extension request concerning Form 20S also constituted an extension request for Form 20SC. The CPA in effect "advised" the Taxpayers that as a matter of law both the 20S and 20SC returns were not due until the extended April 15, 2004 due date. The Taxpayers' reliance on that advice thus constituted reasonable cause. Unlike the situation in *Boyle*, where the attorney failed to file the return because of negligence, the CPA in this case failed to timely file the Form 20SC returns through a misunderstanding of law. The Taxpayers were not negligent in failing to file the returns by a known due date, as in *Boyle*, because they relied on their CPA's advice that as a matter of law, the due date to file the returns had been extended.

The penalty in issue is waived for reasonable cause. The final assessments against Tiger Steak, Inc. and Birmingham I & II Management, Inc. are affirmed for interest only of \$61.10 and \$177.76, respectively. Judgment is entered accordingly.

This Final Order may be appealed to circuit court within 30 days pursuant to Code of Ala. 1975, §40-2A-9(g).

Entered December 28, 2005.

BILL THOMPSON
Chief Administrative Law Judge