

**OFFICE OF TAX APPEALS
STATE OF CALIFORNIA**

In the Matter of the Appeal of:) OTA Case No. 18042779
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JOHNNY PEREZ, JR.) Date Issued: September 24, 2018
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OPINION

Representing the Parties:

For Appellant: Johnny Perez, Jr.
For Respondent: Ricky Martorana, Graduate Student Assistant

J. ANGEJA, Administrative Law Judge: Pursuant to Revenue and Taxation Code section 19045,¹ Johnny Perez, Jr. (appellant) appeals an action by the Franchise Tax Board (FTB or respondent) on appellant’s protest against a proposed assessment in the amount of \$1,579 in additional tax, plus applicable interest, for the 2012 tax year.

Appellant waived his right to an oral hearing and therefore the matter is being decided based on the written record.

ISSUE

Whether appellant’s sick-leave payments are subject to tax.

FACTUAL FINDINGS

1. During the 2012 tax year, appellant was a federal employee and took time off work due to an unspecified illness, using 240 hours of sick leave. The sick-leave payments totaled \$12,772.
2. Appellant filed a timely 2012 California Resident Income Tax Return. On his return, appellant reported federal adjusted gross income (AGI) of \$118,819, California

¹ Unless otherwise indicated, all section references are to sections of the California Revenue and Taxation Code.

adjustments (subtractions) of \$12,772, California AGI of \$106,047, itemized deductions of \$38,182, taxable income of \$67,865, and tax of \$2,553.

3. FTB reviewed appellant's return and on May 11, 2016, issued a Notice of Proposed Assessment (NPA) denying the \$12,772 subtraction from California income and proposing additional tax of \$1,579.² Appellant filed a timely protest, asserting that his sick leave payments are not subject to California tax. On November 30, 2017, FTB issued a Notice of Action that affirmed the NPA. This timely appeal followed.

DISCUSSION

It is well settled that deductions and exclusions are a matter of legislative grace and are allowable only where the conditions established by the legislature have been satisfied. (*New Colonial Ice Co. v. Helvering* (1934) 292 U.S. 435, 440.) Additionally, respondent's determination is presumed correct (*Appeal of Richardson*, 80-SBE-135, Oct. 28, 1980), and appellant bears the burden of proving that he is entitled to the claimed deduction (*Appeal of Gordos*, 82-SBE-062, Mar 31, 1982).³

California personal income tax law provides that exclusions from income are to be determined in accordance with the Internal Revenue Code (IRC). (§ 17131.) IRC section 61 provides that, except as otherwise provided by law, gross income means all income from whatever source derived, including compensation for services. IRC section 104(a)(1) provides several exclusions of "sick pay" from gross income. Among other exceptions, and as herein relevant, IRC section 104 excludes the amounts received under workers' compensation acts, and amounts received through accident or health insurance for personal injuries or sickness (subject to the limitation provided in IRC section 105). (IRC, §§ 104(a)(1), (a)(3).)⁴

The regulation interpreting IRC section 104 provides that payments made under a statute that is in the nature of a workers' compensation act are also excludable from gross income;

² Appellant reported pension income of \$15,929 on his tax return. The proposed, disputed additional tax at issue on appeal of \$1,579 includes an early distribution tax of \$398 imposed on appellant's early distribution from his retirement plan. (Generally, early distributions from qualified retirement plans are taxable, and a 2.5 percent additional tax applies to early distributions. (§ 17085(c)(1).) Appellant has not specifically protested the early distribution tax and therefore we decline to address it.

³ Published decisions of the Board of Equalization, designated by "SBE" in the citation, are available on that Board's website at: <http://www.boe.ca.gov/legal/legalopcont.htm>.

⁴ IRC Section 104 provides additional exceptions that do not appear to be relevant in this appeal, and thus we need not address them. (See IRC § 104(a)(2), (a)(4), (a)(5), and (a)(6).)

however, the exclusion does not apply to amounts received as compensation for an occupational injury or sickness to the extent that they are in excess of the amount provided in the applicable workers' compensation act or acts. (*Appeal of House*, 93-SBE-016, Oct. 28, 1993; Treas. Reg. § 1.104-1(b).) If sick-leave payments are not issued pursuant to a workers' compensation statute, they do not meet the requirements for exclusion under IRC section 104. (*Appeal of House, supra.*)⁵ IRC section 104(a)(3) also excludes from gross income amounts received through accident or health insurance for personal injuries or sickness to the extent that the employee paid for the insurance premiums from his or her own funds. (See also IRC, § 105(a); Treas. Reg. § 1.104-1(d).)

Here, appellant has neither alleged nor established that he received sick-leave payments pursuant to a workers' compensation statute. Although the evidence is unclear, appellant appears to have received his sick-leave payments pursuant to the laws and rules governing the accumulation and use of sick leave by federal employees (see 5 U.S.C. § 6307 *et seq.*). Payments for such sick leave do not require a service-related injury or illness, and therefore we conclude that appellant has failed to establish that his sick-leave payments were made under a workers' compensation statute. Similarly, appellant has neither alleged nor established that his sick-leave payments were made from an insurance plan for which he paid all or a portion of the premiums.

Accordingly, appellant has failed to establish that the sick-leave payments at issue met the requirements for exclusion under IRC section 104.

HOLDING

Appellant has failed to establish that his sick-leave payments are nontaxable.

DISPOSITION

Respondent's action is sustained.

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Jeffrey G. Angeja
Administrative Law Judge

⁵ A statute is essentially a workers' compensation statute only if it allows disability payments solely for service-related personal injury or sickness. (See *Take v. Commissioner* (1984) 82 T.C. 630, 634.)

We concur:

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Teresa A. Stanley
Administrative Law Judge

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Alberto T. Rosas
Administrative Law Judge