

**OFFICE OF TAX APPEALS  
STATE OF CALIFORNIA**

In the Matter of the Appeal of:  <b>KATHERINE S. THURSBY</b>	) ) ) ) ) )	OTA Case No. 18011139  Date Issued: November 7, 2018
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**OPINION**

Representing the Parties:

For Appellant:	Katherine S. Thursby
For Respondent:	Donna L. Webb, Staff Operation Specialist

N. DANG, Administrative Law Judge: Pursuant to Revenue and Taxation Code section 19045,<sup>1</sup> Katherine S. Thursby (appellant) appeals an action by Franchise Tax Board (FTB or respondent) denying her protest of a proposed assessment of \$445 additional tax, plus applicable interest, for the 2011 tax year.<sup>2</sup>

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

**ISSUE**

Was appellant entitled to a \$6,980 California adjustment to (subtraction from) income for the 2011 tax year?

**FACTUAL FINDINGS**

1. Appellant timely filed her 2011 California Resident Income Tax Return, reporting in relevant part, federal adjusted gross income (AGI) of \$137,889, a California subtraction from income of \$6,980 based on a health savings account (HSA) distribution, and tax of

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<sup>1</sup> Unless otherwise specified, all further undesignated statutory “section” or “§” references are to sections of the Revenue and Taxation Code.

<sup>2</sup> As discussed in further detail below, FTB concedes to reduce its original proposed assessment from \$650 to \$445 additional tax.

- \$8,958. After applying a withholding credit of \$10,853, appellant reported an overpayment of \$2,340, which FTB refunded to her on April 26, 2012.
2. Appellant's reported 2011 federal AGI included wages and her prior year state tax refund, but did not include an HSA distribution.
  3. After reviewing appellant's 2011 return, on April 13, 2016, FTB issued to appellant a Notice of Proposed Assessment (NPA) disallowing appellant's claimed subtraction from income of \$6,980, based on information from the Internal Revenue Service (IRS) indicating that appellant's federal AGI for that year did not include an HSA distribution. The NPA proposed additional tax and interest totaling \$712.71.
  4. By letter dated May 2, 2016, appellant protested the NPA. Included with appellant's protest letter was a payment of \$712.71, which satisfied the NPA in full.
  5. On October 18, 2017, FTB responded stating that while appellant is not entitled to a \$6,980 subtraction from income based on her HSA distribution, she may treat that amount as a qualified medical expense, which is deductible to the extent that it exceeds 7.5 percent of her \$137,889 federal AGI (\$10,342). Accounting for an additional \$5,560 in qualified medical expenses which appellant reported on her federal return, FTB allowed appellant a qualified medical expense deduction of \$2,198 ( $\$6,980 + \$5,560 - \$10,342$ ).
  6. Consequently, on November 29, 2017, FTB issued a Notice of Action (NOA) to appellant, revising its proposed assessment from \$650 to \$445 additional tax.<sup>3</sup>
  7. By letter dated December 29, 2017, appellant timely appealed the NOA. This letter also included a claim for refund for appellant's \$712.71 payment made on May 2, 2016.

### DISCUSSION

The law requires FTB to examine returns and determine the correct amount of tax due. (§ 19032.) When FTB determines that the tax disclosed in the original return is less than the tax disclosed by its examination, it has the authority to make a deficiency assessment. (§ 19033.) FTB has the initial burden to show that a proposed assessment is reasonable and rational. (*Appeal of Michael E. Myers*, 2001-SBE-001, May 31, 2001; *Todd v. McColgan* (1949) 89

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<sup>3</sup> FTB's adjustment resulted in an overpayment of \$225.92, of which \$16.36 was applied to appellant's outstanding liability with the California Department of Motor Vehicles. FTB has agreed to refund the balance of the overpayment to appellant after this appeal is resolved.

Cal.App.2d 509.)<sup>4</sup> If FTB satisfies its burden, the proposed assessment is presumed to be correct, and the taxpayer then carries the burden of producing sufficient evidence to overcome this presumption of correctness. (*Ibid.*) Unsupported assertions are not sufficient to satisfy a taxpayer's burden of proof. (*Appeal of Aaron and Eloise Magidow*, 82-SBE-274, Nov. 17, 1982.)

At issue in this appeal is the propriety of appellant's exclusion from gross income of her HSA distribution. Appellant asserts that HSA distributions are not subject to tax, and appellant is correct. California does not allow a deduction from gross income for contributions made to an HSA,<sup>5</sup> and therefore the distributions from an HSA are nontaxable for California purposes because they were already taxed when earned. But that does not resolve the issue before us, which is whether appellant is entitled to exclude her HSA distribution from gross income when that amount was not previously included in her federal AGI.

Federal AGI is the starting point on the return for computing gross income for California purposes, and is further adjusted to remove items of income which are subject to federal but not state tax, such as appellant's HSA distribution. This means that to exclude an item of income on the return, it must first be included in federal AGI. In the instant case, appellant's HSA distribution is not subject to either federal or state tax, and appellant's \$137,889 federal AGI for the 2011 tax year consists entirely of wages and her prior year state tax refund. Therefore, because appellant's HSA distribution was previously excluded from her federal AGI, a California adjustment to income to *again* exclude that HSA distribution from gross income for California purposes was clearly erroneous. Thus, despite appellant's assertion to the contrary, FTB's proposed assessment did not result in her HSA distribution being subject to tax; it merely disallowed the subtraction of an item that did not exist to be subtracted. Hence, we find FTB's

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<sup>4</sup> Published precedential opinions of the State Board of Equalization (BOE) may be found on its website at: <<http://www.boe.ca.gov/legal/legalopcont.htm>>. The Office of Tax Appeals is the successor to, and vested with, all of the duties, powers and responsibilities of the BOE necessary or appropriate to conduct appeals hearings. (Gov. Code, § 15672(a).) Therefore, precedential BOE opinions that were adopted prior to January 1, 2018, are precedential authority before OTA. (Cal. Code Regs., tit. 18, § 30501(d)(3).)

<sup>5</sup> Under federal law, eligible individuals may establish an HSA, which is a tax-exempt trust or custodial account used to pay or reimburse the qualified medical expenses of the account beneficiary and his or her spouse or dependents. (Int.Rev. Code, § 223(d)(1), (2)(a).) HSA *contributions* (which are not at issue here) made by eligible individuals and employers acting on their behalf are excludable from gross income. (Int.Rev. Code, §§ 223(a), 106(d).) However, in a departure from federal law, California requires that HSA contributions be included in gross income. (§§ 17215.4, 17131.4.) In other words, contributions to an HSA are deductible for federal income tax purposes but not for California tax purposes.

determination to be both reasonable and rational. Appellant has neither provided any evidence or contentions refuting the information received by FTB, nor has she provided any other explanation or support for this adjustment. Accordingly, we find that appellant has not met her burden of substantiating her \$6,980 California adjustment to income.

HOLDING

Appellant was not entitled to a \$6,980 California subtraction from income for the 2011 tax year.

DISPOSITION

In accordance with FTB’s NOA dated November 29, 2017, FTB’s proposed assessment is modified to reduce the additional tax from \$650 to \$445. Otherwise, FTB’s action is sustained.

DocuSigned by:  
*Nguyen Dang*  
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Nguyen Dang  
Administrative Law Judge

We concur:

DocuSigned by:  
*Michael F. Geary*  
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Michael F. Geary  
Administrative Law Judge

DocuSigned by:  
*Jeff Angeja*  
0D390BC3CCB14A9...  
Jeffrey G. Angeja  
Administrative Law Judge