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OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

In the Matter of the Appeal of:	) OTA Case No. 18042758
STEVE FERNANDEZ	) Date Issued: November 6, 2019

OPINION

Representing the Parties:

For Appellant: Christopher Engelmann, TAAP

For Respondent: Jean M. Cramer, Tax Counsel IV

T. STANLEY, Administrative Law Judge: Pursuant to California Revenue and Taxation Code (R&TC) section 19045, Steve Fernandez (appellant) appeals an action by respondent Franchise Tax Board (FTB) proposing $6,275 of additional tax, an accuracy-related penalty of $1,255, and applicable interest for taxable year 2012; $7,456 of additional tax, an accuracy-related penalty of $1,491, and applicable interest for taxable year 2013; and additional tax of $5,176, an accuracy-related penalty of $1,035, and applicable interest for taxable year 2014.[1]

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

ISSUES

1. Has appellant established error in FTB's proposed assessments that were based on federal determinations for taxable years 2012, 2013, and 2014?
2. Has appellant established that the accuracy-related penalties assessed for 2012, 2013, and 2014 taxable years should be abated?

FACTUAL FINDINGS

1. Appellant filed timely tax returns reporting itemized deductions exceeding adjusted gross income and zero taxable income, for taxable years 2012, 2013, and 2014.

[1] Amounts are rounded to the nearest $1.00.

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2. On June 10, 2015, FTB received information showing that the Internal Revenue Service (IRS) adjusted appellant's 2012 federal return, including disallowing all claimed medical and dental expense deductions of $42,288 and unreimbursed employee expense deductions of $54,894.
3. On August 10, 2015, FTB received information showing that the IRS adjusted appellant's 2013 federal return, including disallowing all claimed medical and dental expense deductions of $41,878 and unreimbursed employee expense deductions of $64,112.
4. On August 10, 2015, FTB received information showing that the IRS adjusted appellant's 2014 federal return, including disallowing all claimed medical and dental expense deductions of $15,051 and unreimbursed employee expense deductions of $56,124.
5. For each year at issue, the IRS assessed a 20 percent accuracy-related penalty.
6. For each year at issue, FTB issued Notices of Proposed Assessments (NPAs) proposing additional tax based on the federal adjustments and assessed a 20 percent accuracy-related penalty.
7. Appellant protested the proposed assessments and requested additional time to provide documentation.
8. IRS Account Transcripts for each taxable year at issue show that, as of January 24, 2017, the federal examinations of appellant's returns were closed, and all federal tax liabilities were paid in full by the end of 2015.
9. Appellant produced a letter from himself "To whom it may concern" requesting a re-audit for each of the three taxable years based on the federal tax auditor's denial of the claimed deductions. In another letter, appellant wrote that he had requested a re-audit from the IRS.[2]
10. Appellant provided no further documentation that the IRS had re-audited any of the taxable years at issue, nor that the IRS had modified or canceled the federal tax liabilities. FTB issued Notices of Action for 2012, 2013, and 2014, which confirmed the NPAs.
11. On appeal, appellant provided an undated and unsigned list of medical expenses broken into four general categories. In addition, appellant provided a statement under penalty of perjury that the list constituted his medical expenses for the three taxable years at issue.

[2] The letter was also written "To whom it may concern," but presumably this was sent to FTB with a copy of his IRS re-audit request letter.

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DISCUSSION

Issue 1 - Has appellant established error in FTB's proposed assessments that were based on federal determinations for taxable years 2012, 2013, and 2014?

R&TC section 18622(a) provides that taxpayers shall report federal adjustments to FTB and either concede the accuracy of a federal determination or state why it is erroneous. A deficiency assessment based on a federal audit report is presumptively correct, and the taxpayer bears the burden of proving that the determination is erroneous. (*Todd v. McColgan* (1949) 89 Cal.App.2d 509, 514; *Appeal of Brockett* (86-SBE-109) 1986 WL 22731.)

The evidence in the appeal record shows that the IRS adjusted appellant's 2012, 2013, and 2014 tax returns, and that FTB followed those adjustments when it proposed assessments and penalties for each of the three years. Although appellant provided evidence that he requested a re-audit, there is nothing showing that such a re-audit was performed. In fact, as of August 6, 2018, the last notations on appellant's federal account transcripts occurred in December 2015. We find that appellant has failed to show that the federal determination upon which FTB relied in making its proposed assessment has been cancelled or revised. Therefore, in order to prevail on this appeal, appellant must show that FTB erred in following the federal determination of appellant's claimed deductions.

Appellant has provided no documentation to support an error in the federal determination with respect to the bulk of the disallowed deductions, including the claimed unreimbursed employee expenses and moving costs. The remaining claim made by appellant is that he is entitled to deductions for medical expenses incurred during each of the three years at issue. Appellant asserts that FTB should allow the medical expense deductions based on the list provided on appeal and the declaration under penalty of perjury attesting to the accuracy of the expenditures on the list.

Income tax deductions are a matter of legislative grace, and a taxpayer who claims a deduction has the burden of proving, by competent evidence, entitlement to that deduction. (*New Colonial Ice Co. v. Helvering* (1934) 292 U.S. 435, 440.) To sustain the burden of proof, a taxpayer must be able to point to an applicable deduction statute and show that he or she came within its terms. (*Appeal of Briglia* (86-SBE-153) 1986 WL 22833.) Unsupported assertions cannot satisfy a taxpayer's burden of proof. (*Appeal of Magidow* (82-SBE-274) 1982 WL 11930.) A taxpayer's failure to produce evidence that is within his or her control gives rise to a

presumption that such evidence, if provided, would have been unfavorable to the taxpayer's case. (*Appeal of Cookston* (83-SBE-048) 1983 WL 15434.)

Internal Revenue Code (IRC) section 213 generally allows taxpayers a deduction for "the expenses paid during the taxable year, not compensated for by insurance or otherwise, for medical care of the taxpayer, his spouse, or a dependent . . . to the extent that such expenses exceed 10 percent of adjusted gross income." (IRC, § 213(a).) This deduction is incorporated into California law by R&TC section 17201. R&TC section 17241(a) substitutes 7.5 percent for 10 percent, so medical expenses are deductible in California to the extent that such amounts exceed 7.5 percent of a taxpayer's adjusted gross income.

Appellant claims significant amounts of medical expenses ($25,212 for 2012, $15,824, for 2013, and $26,288 for 2014). However, the only support for these expenditures is an unsigned, undated list that breaks the expenses into four categories. There is not a single receipt, canceled check, medical invoice, or other evidence that the expenses were actually incurred. In addition, even had appellant offered evidence of the expenses, the information would be incomplete without evidence that none of the claimed expenses were paid by insurance or reimbursed to appellant. Appellant has therefore not met the burden to prove error in FTB's proposed assessments.

Issue 2 - Has appellant established that the accuracy-related penalties assessed for 2012, 2013, and 2014 taxable years should be abated?

When FTB assesses an accuracy-related penalty based on a federal action, the assessment of the penalty is presumptively correct. (*Appeal of Abney* (82-SBE-104) 1982 WL 11781.) R&TC section 19164, which incorporates the provisions of IRC section 6662, provides for an accuracy-related penalty of 20 percent of an underpayment. IRC section 6662(b) provides, in part, that the penalty applies to the portion of the underpayment attributable to: (1) negligence or a disregard of rules and regulations; or (2) any substantial understatement of income tax. IRC section 6662(c) defines "negligence" to include "any failure to make a reasonable attempt to comply" with the provisions of the IRC. The term "disregard" is defined to include any "careless, reckless, or intentional disregard." (*Ibid*.) IRC section 6662(d)(1) provides that a substantial understatement of tax exists if the amount of the understatement exceeds the greater of 10 percent of the tax required to be shown on the return or $5,000. An "understatement"

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means the excess of the amount required to be shown on the return for the taxable year over the tax imposed, reduced by any rebate. (IRC, § 6662(d)(2).)

For each of the taxable years at issue, the IRS imposed accuracy-related penalties. In this case, appellant made substantial understatements of more than $5,000 and more than 10 percent of the tax required to be shown on the return.[3] FTB properly imposed the accuracy-related penalties.

There are three exceptions to the imposition of the accuracy-related penalty. The taxpayer bears the burden of proving any defenses to the imposition of the accuracy-related penalty. (*Recovery Group, Inc. v. Commissioner*, T.C. Memo. 2010-76.)

None of the statutory exceptions to the imposition of the accuracy-related penalty apply here. Appellant does not contend, and the evidence does not show, that there was substantial authority for the tax treatment of any disallowed item. (See IRC, § 6662(d)(2)(B).) Nor has appellant shown any disallowed item's tax treatment was adequately disclosed, or that he had a reasonable basis for the tax treatment of such item. (See *ibid*; Treas. Reg. § 1.6662- 3(c)(1).) He simply failed to substantiate his claimed deductions. In addition, appellant provides no argument or evidence establishing that he acted reasonably and in good faith in determining the tax liabilities. (See IRC, § 6664(c)(1); Treas. Reg. §§ 1.6664-1(b)(2) and 1.6664-4.)

FTB's imposition of the accuracy-related penalties is presumed correct. On appeal, appellant merely contends that the auditor should have allowed his deductions and therefore the penalties should not apply. No supporting evidence was submitted. Accordingly, appellant has failed to establish that the accuracy-related penalties should be abated.

[3] For 2012, appellant reported alternative minimum tax of $385, and was required to report $6,660. For 2013, appellant reported alternative minimum tax of $411, and was required to report $7,867. For 2014, appellant reported tax of $0, and was required to report $5,176.

HOLDINGS

1. Appellant did not establish error in FTB's proposed assessments that were based on federal determinations for taxable years 2012, 2013, and 2014.
2. Appellant did not establish that the accuracy-related penalties assessed for 2012, 2013, and 2014 taxable years should be abated.

DISPOSITION

FTB's actions are sustained in full.

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Teresa A. Stanley
Administrative Law Judge

We concur:

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Sara A. Hosey
Administrative Law Judge

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Josh Lambert
Administrative Law Judge