

**OFFICE OF TAX APPEALS**  
**STATE OF CALIFORNIA**

In the Matter of the Appeal of: ) OTA Case No. 18011120  
**KEN CHANGLIAO** )  
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**OPINION**

Representing the Parties:

For Appellant: Ken Changliao

For Respondent: David Hunter, Tax Counsel IV

A. KWEE, Administrative Law Judge: Pursuant to California Revenue and Taxation Code (R&TC) section 19045, Ken Changliao (appellant) appeals an action by respondent Franchise Tax Board (FTB) in proposing additional tax in the amount of \$7,284, plus interest, for the 2013 tax year. This matter is being decided based on the written record because appellant waived the right to an oral hearing.

**ISSUE**

Whether appellant established a basis to exclude \$87,354 in unreported income from his taxable income?

**FACTUAL FINDINGS**

1. Ridgerock Tools, Inc. (Ridgerock) is a wholesale distributor of miscellaneous power and hand tools such as saws and saw blades.
2. On November 20, 2012, Ridgerock offered appellant a salaried position within the corporation. The details of appellant's role within the corporation are not clear from the evidence in the record; however, his duties included certain web-related services.

3. PayPal, Inc. (PayPal) issued a Form 1099-K to appellant, reporting that it made gross payments of \$87,354 to him during 2013.<sup>1</sup>
4. On April 15, 2014, appellant timely filed a 2013 California Resident Income Tax Return (Form 540) reporting taxable income of \$46,214. Appellant's reported taxable income consisted of: \$53,687 in wages from Ridgerock; \$339 in business income from performing web design services as an independent contractor for Next Generation Logistics, Inc.; less California's standard deduction of \$7,812. Appellant did not include the \$87,354 reported on the Form 1099-K.
5. Appellant separately filed a timely Federal Individual Income Tax Return (Form 1040) reporting federal adjusted gross income (AGI) of \$54,016, and taxable income of \$37,276, and also failing to report the \$87,354 from PayPal.
6. The Internal Revenue Service (IRS) reviewed appellant's return for unreported income due to the Form 1099-K that PayPal furnished to the IRS. Based on its review, the IRS determined that appellant failed to report all of his gross income on his 2013 federal income tax return. The IRS made a \$82,459 adjustment to appellant's federal AGI and taxable income, increasing them to \$136,485 and \$119,735, respectively. The IRS adjustment included a \$4,895 self-employment tax deduction (\$87,354 - \$4,895 = \$82,459).
7. On November 9, 2015, the IRS assessed taxes, interest, and an accuracy-related penalty in connection with the federal adjustment. The IRS also reported to FTB that it had made this adjustment to appellant's 2013 federal tax return.
8. FTB issued a Notice of Proposed Assessment (NPA) on December 9, 2016, making the same adjustment at the state level that the IRS made at the federal level, with the exception that FTB did not add an accuracy-related penalty. The NPA proposes additional tax of \$7,284, plus interest.
9. On February 3, 2017, appellant protested the NPA, asserting that this was not his income, and that he has "no association with the taxpayer [to] whose income [the PayPal

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<sup>1</sup> Federal Form 1099-K, "Payment Card and Third Party Network Transactions," is a form used by credit card companies and third-party processors (payment settlement agencies) to report the gross amount of reportable payments made to the taxpayer by the payment settlement agency. The gross amount of a reportable payment does not include any adjustments for credits, cash equivalents, discount amounts, fees, refunded amounts, or any other amounts. (See <<https://www.irs.gov/businesses/understanding-your-form-1099-k>>.)

- payments] belong.” FTB responded, requesting information on the identity of the taxpayer the income belongs to, or documentation that the IRS adjusted its determination.
10. FTB denied the protest on August 21, 2017, when appellant failed to respond to FTB’s request for additional information. This timely appeal followed.
  11. By letter dated August 27, 2018, the Office of Tax Appeals (OTA) noted that the Internal Revenue Code (IRC), to which California conforms, allows a deduction for all the necessary and ordinary business expenses paid or incurred during the taxable year in carrying on a trade or business. (See R&TC, § 17201; IRC, § 162.) OTA thereafter requested documentation on any business expenses paid during 2013, in connection with generating the PayPal income at issue in this appeal.
  12. Appellant responded to OTA’s request for additional briefing, but failed to provide documentation for a single expense incurred during 2013.<sup>2</sup> Instead, appellant provided a document titled “eBay business plan” that he prepared for Ridgerock during the course of his employment, explaining that Ridgerock’s “mission is to control the price [of its products] on the eBay market and eliminate eBay sellers who sell at very low price[s].” In support, appellant contends that Ridgerock hired him to assist Ridgerock in transitioning out of the wholesale market and “to go direct to retail in 2013 which can give them more control over their own products.” Thus, appellant contends that he made eBay sales on behalf of Ridgerock, and accepted payments via PayPal. Appellant further contends that since the corporation’s inception, Ridgerock’s website has never listed a price for its own products or allowed retail purchases from its website; instead, the website only serves as a catalog for wholesale customers.

### DISCUSSION

Gross income means all income from whatever source derived, unless specifically excluded. (R&TC, § 17071; IRC, § 61(a).) The taxpayer bears the burden of establishing entitlement to any deductions claimed. (*Appeal of Janke* (80-SBE-059) 1980 WL 4988; *Appeal*

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<sup>2</sup> The only document potentially relevant to deductible expenses that appellant furnished, without any explanation as to its relevance, was a printed excel spreadsheet listing approximately 45 sale transactions (PayPal reported 2,870 transactions for appellant’s account during 2013). The 45 transactions generated \$776.17, including \$7.32 in “sales tax” collected from five customers. Information such as the name of the seller, date of sale, year of sale, or method payment was not provided. There is no evidence that these sales occurred during 2013, or explanation of how they are relevant to this appeal. As such, we do not discuss this document further.

*of Walshe* (75-SBE-073) 1975 WL 3557.) If the IRS makes a change or correction to any item of gross income or deduction, the taxpayer must report the federal change to FTB within six months after the date it becomes final and shall concede the accuracy of the final federal determination or state wherein it is erroneous. (R&TC, § 18622(a).) The date of each final federal determination is the date the IRS assesses the tax within the meaning of IRC section 6203 (which provides that the IRS shall record the liability of the taxpayer pursuant to the applicable rules and regulations). (IRC, § 18622(d).) An NPA issued by FTB based on a final federal determination is presumed correct, and the taxpayer bears the burden of proving error. (*Todd v. McColgan* (1949) 89 Cal.App.2d 509; *Appeal of Brockett* (86-SBE-109) 1986 WL 22731.)

As a preliminary matter, PayPal reported paying a total of \$87,354 in 2013 to an individual with an identical name, social security number, and home address as which appellant used when he filed his state and federal tax income returns. Appellant provided no documentation to support his initial claim that he had no association with the person generating this income, and we find no evidence in the record to support reaching such a conclusion.

To the contrary, it appears appellant now admits that he made at least some of the sales generating this income on behalf of Ridgerock. Appellant contends that he was merely a middleman, and forwarded the PayPal payments he collected to Ridgerock. Appellant provides three checks, one each from September, October, and November of 2013, showing payments from him to Ridgerock in the amounts of \$6,934.54, \$4,420.88, and \$5,663.05, respectively.<sup>3</sup> Appellant has not provided any agreement authorizing him to sell Ridgerock's products online, or collect payments on behalf of the corporation. Furthermore, Ridgerock is a corporation and appellant failed to explain why a corporation would provide appellant's social security number, instead of the corporation's own taxpayer identification number, when registering for a financial account intended to be used to collect payments received by the corporation.<sup>4</sup> Finally, the check amounts are substantially lower than what would be correlating amounts reported on the 1099-K

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<sup>3</sup> For comparison, the Form 1099-K shows payments to appellant totaling \$12,313; \$9,282; and \$15,062 for September through November of 2013, respectively.

<sup>4</sup> As relevant, appellant contends that he used his eBay account to make sales because new eBay accounts require a probation period. It is important to note here that the NPA is based entirely on unreported PayPal income. There is insufficient evidence in the record to tie any of the unreported income to eBay sales. Furthermore, even if it were established that the PayPal income originated from eBay sales; eBay and PayPal are entirely separate and distinct entities and there is still no explanation for why a corporation would use appellant's PayPal account (and social security number) to collect payments. It's also unclear how Ridgerock could establish its own eBay selling account, as appellant contends it hired him to do, if it was relying on appellant's eBay account to make sales.

(i.e., \$17,018.47 in checks compared to \$87,354 in PayPal income). There is also no information written on the checks that would support the existence of such an agreement. Therefore, we find that appellant's contention that he was acting as a middle-man for Ridgerock is unsupported by the evidence.

Appellant offers no argument or contention that the checks are otherwise deductible business expenses, such as cost of goods sold. Furthermore, there is no evidence that links the checks that appellant paid to Ridgerock with the income that appellant received via PayPal. Thus, for example, we have no way of ascertaining whether the check payments were costs of goods sold, personal purchases, or an unrelated item of expense or reimbursement between the parties. Therefore, we find that appellant failed to establish that the three payments he made to Ridgerock are relevant to this appeal.

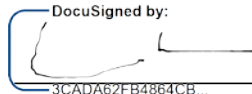
In conclusion, it is undisputed that appellant failed to report any portion of the \$87,354 from PayPal as income on his state or federal income tax returns. Gross income means all income from whatever source derived, including compensation for services (which includes fees, commissions, fringe benefits, and similar items). (R&TC, § 17071; IRC, § 61(a)(1).) Therefore, we find that appellant earned the \$87,354 in gross income as reported on the Form 1099-K. Appellant's gross income is includable in taxable income unless it is otherwise deductible. (R&TC, § 17073; IRC, § 63.) Nevertheless, appellant failed to sufficiently document a single business expense incurred during 2013, even though we specifically requested this information from appellant and allowed appellant additional time to submit such documentation. The NPA made the same inclusions to gross income and allowed the same deductions as the IRS assessment, and California conforms to federal law on these items. Therefore, we find that appellant failed to establish error with the NPA or the federal determination upon which it is based.

HOLDING

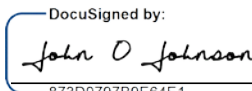
Appellant has not shown that unreported income of \$87,354 should be excluded from his taxable income.

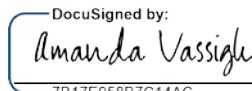
DISPOSITION

FTB's proposed assessment for the 2013 tax year is sustained.

DocuSigned by:  
  
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Andrew J. Kwee  
Administrative Law Judge

We concur:

DocuSigned by:  
  
873D8797B9E64E1  
John O. Johnson  
Administrative Law Judge

DocuSigned by:  
  
7B17E958B7C14AC  
Amanda Vassigh  
Administrative Law Judge

Date Issued: 1/17/2020