OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

In the Matter of the Appeal of: **J. LIU AND** **N. MUKAE**	) OTA Case No. 18103867)))))

OPINION

Representing the Parties:

For Appellants: J. Liu

For Respondent: Brian Werking, Tax Counsel III

E.S. EWING, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19045, J. Liu and N. Mukae (appellants) appeal an action by respondent Franchise Tax Board proposing additional tax of $2,407, plus applicable interest, for the 2013 tax year.

Office of Tax Appeals Administrative Law Judges Elliott Scott Ewing, Kenneth Gast, and Daniel K. Cho held an oral hearing for this matter on March 16, 2021.[1] At the conclusion of the oral hearing, we closed the record and this matter was submitted for decision.

ISSUE

Whether appellants have shown error in respondent's proposed assessment, which is based on a final federal determination.

[1] The oral hearing was conducted electronically due to COVID-19.

FACTUAL FINDINGS

1. Appellants filed a joint 2013 California Resident Income Tax Return, which incorporated tax information they reported on their 2013 federal income tax return.
2. Subsequently, the Internal Revenue Service (IRS) audited appellants' 2013 federal income tax return and disallowed certain unreimbursed employee expenses of $25,869 that appellants claimed as miscellaneous itemized deductions.[2] This adjustment increased appellants' federal taxable income by the same amount, resulting in additional regular tax of $6,543.[3] However, this additional regular tax was offset by a corresponding reduction of the same amount to appellants' federal alternative minimum tax (AMT), resulting in no net increase to appellants' overall federal income tax due for the 2013 tax year.
3. Based on this federal information, respondent issued a Notice of Proposed Assessment (NPA) for the 2013 tax year, increasing appellants' California taxable income by the same amount the IRS increased appellants' federal taxable income – i.e., $25,869 – and proposing additional tax of $2,407, plus applicable interest.[4]
4. Appellants protested the NPA. At the conclusion of the protest, respondent issued a Notice of Action affirming the NPA. This timely appeal followed.

DISCUSSION

R&TC section 18622(a) requires taxpayers to concede the accuracy of a federal determination or to state where the change is erroneous. It is well settled that respondent's proposed assessment based on a federal determination is presumptively correct and taxpayers bear the burden of proving that the determination is erroneous. (*Appeal of Gorin*, 2020-OTA-018P.) Generally, the applicable burden of proof is by a preponderance of the evidence. (Cal. Code Regs., tit. 18, § 30219(c).) That is, taxpayers must establish by documentation or other evidence that the circumstances they assert are more likely than not to be correct. (*Appeal of*

[2] We note the IRS documents in the record, such as the FEDSTAR IRS Data Sheet dated August 5, 2016, indicate the federal adjustment is $25,870, or $1 greater than $25,869, but we use the latter number because that is what respondent's proposed assessment is based on.

[3] Appellants' federal taxable income was increased from $125,691 to $151,561.

[4] This additional California income tax was not offset by a corresponding reduction to appellants' California AMT because they were not subject to AMT for California tax purposes.

Estate of Gillespie, 2018-OTA-052P, fn. 6.) Unsupported assertions are not sufficient to satisfy taxpayers' burden of proof with respect to an assessment based on a federal action. (*Appeal of Gorin*, *supra*.) In the absence of credible, competent, and relevant evidence showing that respondent's determination is incorrect, it must be upheld. (*Appeal of Mazer*, 2020-OTA-263P.) R&TC section 17201 incorporates Internal Revenue Code section 162(a), which authorizes a deduction for all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including certain unreimbursed employee expenses. (See Treas. Reg. § 1.162-17(a).)

Appellants argue that the IRS only "proposed" to disallow their unreimbursed employee expenses of $25,869, but it did not actually make that adjustment and therefore their federal taxable income for 2013 was not increased by that amount. Further, appellants assert that they were told by IRS personnel that the IRS was experiencing an internal computer "system glitch" that prevented it from updating the records to reverse the proposed expense disallowance of $25,869. Appellants further assert that the IRS did "manually adjust" their 2013 account to reduce their additional tax liability to zero. However, appellants are unable to provide a letter or other correspondence from the IRS substantiating the asserted adjustment. Accordingly, we find that there is no evidence to support appellants' assertions.

Moreover, the record does not show that the IRS withdrew or otherwise revised its disallowance of appellants' claimed unreimbursed employee expenses. Instead, the record shows that because the IRS disallowed these expenses, appellants' regular federal tax increased which, by operation of the interplay between the calculation of the regular income tax and the AMT, had the effect of decreasing their federal AMT by exactly the same amount. This resulted in no additional federal income tax due. Several evidentiary documents support this. For example, appellants' federal Account Transcript—which is dated February 6, 2019, and one of the more recent IRS documents in the record—indicates that their federal adjusted gross income for 2013 was increased by the IRS to $151,561, which corresponds with the disallowed unreimbursed employee expenses at issue here. The IRS Examining Officer's Activity Record contains an entry dated June 8, 2016, that states "[w]hen the corrections were made[,] the AMT zero outs [sic] the deficiency of the 2013 tax return." Therefore, the IRS case was forwarded "for closure as a Change/No Change case." IRS audit workpaper lead sheets dated March 31, 2016, indicate that appellants "did not provide any invoices or receipts to

substantiate" the unreimbursed employee expenses paid. In addition, IRS Form 4549, Income Tax Examination Changes, dated June 8, 2016, indicates that the IRS did not revise its federal adjustment disallowing $25,869, even though it resulted in no additional federal tax.

For these reasons, in addition to the fact that appellants have not otherwise substantiated the claimed unreimbursed employee expenses of $25,869, we find appellants have failed to carry their burden of showing they are entitled to deduct these expenses on their 2013 California tax return.

HOLDING

Appellants have not shown error in respondent's proposed assessment, which is based on a final federal determination.

DISPOSITION

Respondent's action is sustained in full.

DocuSigned by:
E.S.Ewing
2D8DE82EB65E4A6...
Elliott Scott Ewing
Administrative Law Judge

We concur:

DocuSigned by:
Kenneth Gast
4283B8CD40F34BC...
Kenneth Gast
Administrative Law Judge

DocuSigned by:
Daniel Cho
7B28A07A7E0A43D...
Daniel K. Cho
Administrative Law Judge

Date Issued: 5/13/2021