

OFFICE OF TAX APPEALS
STATE OF CALIFORNIA

In the Matter of the Appeal of:) OTA Case No. 21067963
)
C. DENCKLAU AND)
H. DENCKLAU)
)
)

OPINION

Representing the Parties:

For Appellants:	C. Dencklau and H. Dencklau
For Respondent:	Darren Ewing, Graduate Legal Assistant
For Office of Tax Appeals:	Lisa Burke, Business Taxes Specialist III

O. AKOPCHIKYAN, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19045, C. Dencklau (appellant-husband) and H. Dencklau (appellant-wife) (together, appellants) appeal an action by respondent Franchise Tax Board (FTB) proposing additional tax of \$2,318.00, plus interest, for tax year 2016.¹

Appellants waived the right to an oral hearing; therefore, this appeal is decided on the written record.

ISSUE

Whether appellants' California taxable income includes the entire amount of resident appellant-wife's California wage income and appellant-wife's community property share (50 percent) of nonresident appellant-husband's income earned outside of California.

¹ Appellants' request for appeal indicates the total amount in controversy is \$585.92. However, we believe the total amount in controversy is \$2,318.00, plus interest, as reflected on FTB's Notice of Action. While appellants' request for appeal indicates they are willing to concede that 50 percent of nonresident appellant-husband's out-of-state wages are taxable in California, their concession is conditioned on FTB's concession that 50 percent of resident appellant-wife's California wages are not taxable in California. FTB has made no such concession. Therefore, the total amount reflected on FTB's Notice of Action is in controversy.

FACTUAL FINDINGS

1. In 2016, appellant-husband was a Texas resident and domiciliary and earned his W-2 wages working outside of California. In 2016, appellant-wife was a California resident and Texas domiciliary and earned her W-2 wages working in California.
2. Appellants timely filed a joint Form 540NR, California Nonresident or Part-Year Resident Income Tax Return, for tax year 2016. Appellants excluded the entirety of appellant-husband's out-of-state wages from their California taxable income.
3. After examining appellants' 2016 return, FTB determined that appellants' California taxable income includes not only appellant-wife's California wages, but also her one-half community property share (50 percent) of appellant-husband's out-of-state wages.
4. FTB subsequently issued a Notice of Proposed Assessment, which was affirmed by a Notice of Action.
5. Appellants timely filed this appeal.

DISCUSSION

California residents, such as appellant-wife, are taxed on all of their income regardless of source. (R&TC, § 17041(a).) California nonresidents, such as appellant-husband, are taxed only on income from California sources. (R&TC, §§ 17041(b) & (i), 17951.)

Appellants contend that only 50 percent of their combined income is subject to California tax because (1) their combined income is community property and should be divided equally, and (2) appellant-husband was not a resident of California in 2016. We disagree.² “[W]here one spouse is a resident of California and the other spouse is a nonresident of California, the determination of whether an item of income is taxable in California to the nonearning spouse can be broken down into a two-step analysis” (*Appeals of Cremel and Koepfel*, 2021-OTA-222P, at p. 5 (*Cremel*)). “The first step requires a determination of the nonearning spouse’s marital property interest in the earning spouse’s income.” (*Ibid.*) “An individual’s marital property interest in personal property [including wages] is determined by the laws of the earning or acquiring spouse’s domicile.” (*Cremel, supra*, at p. 5.) “If the nonearning spouse has a marital property interest in the earning spouse’s income, the second step requires a

² Appellants’ position is that 50 percent of their combined income is subject to California tax. FTB’s action results in approximately 61 percent of the combined income subject to California tax.

determination of whether the nonearning spouse’s interest in such income is taxable in California.” (*Ibid.*) “The nonearning spouse’s marital property interest in the income may be taxable in California either because the nonearning spouse is a resident of California who is taxed on all income regardless of source (R&TC, § 17041(a)), or because the nonearning spouse is a nonresident, but the income is California source income (R&TC, §§ 17041(b) & (i) and 17951).” (*Ibid.*)

With respect to appellant-wife’s California wages, appellant-husband has a one-half community property interest in that income because appellant-wife, the earning spouse, was domiciled in Texas, a community property state.³ (Tex. Fam. Code, § 3.002(a).) Appellant-wife’s California wages is California sourced income in appellant-husband’s hands because appellant-wife performed services in California to earn that income. (See Cal. Code Regs., tit. 18, § 17951-5.) California nonresidents, such as appellant-husband, are subject to tax on California sourced income. (R&TC, §§ 17041(b) & (i) and 17951.) In addition, appellant-wife’s one-half community property interest in her wages is also taxable in California because she was a California resident and subject to tax on all income, regardless of source. (R&TC, § 17041(a).) Thus, the entirety of appellant-wife’s California wages is subject to California tax.

With respect to appellant-husband’s out-of-state wages, appellant-wife has a community property interest in that income because appellant-husband was also domiciled in Texas, a community property state.⁴ (Tex. Fam. Code, § 3.002(a).) Appellant-wife’s community property interest is taxable in California because appellant-wife was a California resident and subject to tax on all income, regardless of source—including her one-half community property interest in appellant-husband’s out-of-state wages. (See R&TC, § 17041(a); see also *Appeal of Misskelley* (84-SBE-077) 1984 WL 16156 [California resident spouse liable for California income tax on share of out-of-state earnings of nonresident spouse domiciled in a non-California community property state].) However, appellant-husband’s community property share of his out-of-state wages is not taxable in California.

³ There is no evidence in the record to suggest appellants had an agreement declaring appellant-wife’s California wages as her separate property.

⁴ There is no evidence in the record to suggest appellants had an agreement declaring appellant-husband’s out-of-state wages as his separate property.

HOLDING

Appellants’ California taxable income includes the entire amount of resident appellant-wife’s California wage income and appellant-wife’s community property share (50 percent) of nonresident appellant-husband’s income earned outside of California.

DISPOSITION

FTB’s action is sustained.

DocuSigned by:
Ovsep Akopchikyan
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Ovsep Akopchikyan
Administrative Law Judge

We concur:

DocuSigned by:
Kenneth Gast
3AF5C32BB93B456...
Kenneth Gast
Administrative Law Judge

DocuSigned by:
Cheryl L. Akin
1A8C8E38740B4D5...
Cheryl L. Akin
Administrative Law Judge

Date Issued: 3/29/2022