

**OFFICE OF TAX APPEALS
STATE OF CALIFORNIA**

In the Matter of the Appeal of:)
M. BARTA AND) OTA Case No. 21017171
T. BACHOR)
_____)

OPINION

Representing the Parties:

For Appellants: Scott B. Price, CPA
Krishnaveni M. Nalla Kumar, EA
For Respondent: Kristin K. Yeager, Program Specialist

T. STANLEY, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19045, M. Barta (appellant-wife) and T. Bachor (appellant-husband), collectively (appellants), appeal an action by respondent Franchise Tax Board (FTB) proposing additional tax of \$927, and applicable interest, for the 2016 taxable year.

Appellants waived the right to an oral hearing; therefore, the Office of Tax Appeals (OTA) decides the matter based on the written record.

ISSUE

Have appellants established error in FTB’s proposed assessment of additional tax that is based on a federal determination?

FACTUAL FINDINGS

1. On their federal tax return, appellants reported individual retirement account (IRA) distributions totaling \$15,724, which were reported to appellant-wife on two federal Forms 1099-R (Distributions from Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.) from Charles Schwab & Co., Inc. (Charles Schwab). One Form 1099-R issued to appellant-wife reported gross distributions of \$5,724 and reported \$0 as taxable (first Form 1099-R). The second Form 1099-R issued

- to appellant-wife reported gross distributions of \$10,000 and reported \$10,000 as taxable (second Form 1099-R). Appellants claimed \$34 of the IRA distributions as taxable income on their 2016 federal tax return.
2. Appellants submitted two federal Forms 5498 (IRA Contribution Information) issued in appellant-wife's name. The first Form 5498 reports IRA contributions totaling \$5,500 for the 2016 taxable year. The first Form 5498 also reports recharacterized contributions of \$5,724.70 (the amount reported as nontaxable on the first Form 1099-R), a fair market value of \$1,037.86, and no Roth IRA conversion amount. The second Form 5498 reports a Roth IRA conversion amount of \$10,000 (the amount reported as taxable on the second Form 1099-R) and reports no contributions for 2016.
 3. Appellants filed a timely California tax return reporting federal adjusted gross income (AGI) that included only \$34 of IRA distributions made to appellant-wife by Charles Schwab.
 4. Subsequently, FTB received information from the IRS showing that the IRS adjusted appellants' federal AGI, increasing it by \$9,963, to reflect a \$10,000 total taxable pension or annuity (retirement account) distribution from Charles Schwab.¹
 5. FTB made corresponding adjustments to appellants' California AGI and issued a Notice of Proposed Assessment (NPA) proposing additional tax of \$927 plus interest.
 6. Appellants protested the NPA. FTB issued a Notice of Action denying the protest. This timely appeal followed.
 7. On appeal, appellants provided a copy of an amended federal return with a partially completed federal Form 8606 (Nondeductible IRAs) attached, which appellants contend were provided to the IRS.
 8. As of March 2, 2022, appellants' 2016 federal account transcript shows that they filed multiple amended returns, with the last one filed on September 27, 2021.² The transcript

¹ The information provided by the IRS shows total distributions of \$10,000, which corresponds with appellant-wife's federal Wage and Income Transcript. The IRS adjustment, however, was in the amount of \$9,997 less the \$34 appellants claimed as taxable income, for a total increase to AGI of \$9,963. The \$3 discrepancy was carried over by FTB and is in appellants' favor, so OTA does not address it further.

² Appellants' federal account transcript shows that appellants filed amended federal returns on May 5, 2020, May 7, 2020, August 8, 2020, and September 27, 2021. However, appellants submitted only one copy of an amended federal return on appeal. Nothing in OTA's record shows whether the same amended return was filed with the IRS more than once, or whether appellants filed separate amended returns.

shows that the IRS did not reduce or cancel its assessment. The IRS disallowed appellants' claim(s), once on November 8, 2021, and a second time on January 17, 2022, which is the last entry for appellants' 2016 taxable year. According to the transcript, appellants' federal AGI includes the additional income of \$9,963.

DISCUSSION

R&TC section 18622(a) provides that if the IRS changes or corrects any item required to be shown on a federal tax return, a taxpayer must report each change or correction within six months of the final federal determination and concede the accuracy of the determination or state wherein it is erroneous. If the federal determination increases the taxpayer's federal personal income tax liability, the determination will also increase the taxpayer's California personal income tax liability to the extent California law follows federal law. (See *Ordlock v. Franchise Tax Board* (2006) 38 Cal.4th 897, 901.) It is well settled that a deficiency assessment based on federal adjustments to income is presumptively correct, and a taxpayer bears the burden of proving that the determination is erroneous. (*Appeal of Valenti*, 202-OTA-093P.) In the absence of credible, competent, and relevant evidence showing that FTB's determination is incorrect, the determination must be upheld. (*Ibid.*)

Gross income means all income from whatever source derived, unless specifically excluded. (R&TC § 17071; Int.Rev. Code (IRC), § 61(a).) Generally, a distribution from a qualified retirement plan, such as an IRA, is included in income for the year of distribution. (IRC, §§ 402(a) & 408(d).)³ Deductions from gross income are a matter of legislative grace, and a taxpayer has the burden of proving entitlement to the deductions claimed. (*New Colonial Ice Co. v. Helvering* (1934) 292 U.S. 435; *Appeal of Dandridge*, 2019-OTA-458P.) To carry the burden of proof, the taxpayer must point to an applicable statute and show by credible evidence that the deductions claimed come within its terms. (*Appeal of Jindal*, 2019-OTA-372P.) Unsupported assertions are not sufficient to satisfy a taxpayer's burden of proof. (*Appeal of Porreca*, 2018-OTA-095P.)

Here, FTB obtained information from the IRS that appellants' joint 2016 federal taxable income had been increased based on a distribution made by Charles Schwab to appellant-wife (reported on the second Form 1099-R). FTB made conforming adjustments to appellants' joint

³ California conforms to IRC sections 402 and 408 pursuant to R&TC section 17501(a).

2016 California tax return, which resulted in the proposed assessment. Based on these federal adjustments, FTB's proposed assessment is presumed correct. Therefore, it is appellants' burden of proof to show that the proposed assessment is erroneous.

On appeal, appellants argue that they filed an amended federal tax return, requesting to cancel or modify the IRS determination. OTA extended the briefing times for this appeal for 90 days, on two separate occasions, to give the IRS time to review appellants' amended federal returns. Appellants did not submit any documentation showing that the IRS cancelled or modified its determination. Instead, at OTA's request, FTB submitted appellants' current federal account transcript for 2016, dated March 2, 2022, which shows that the IRS denied appellants' claims. As a result, OTA concludes that appellants have not established that the federal determination was cancelled or reduced such that FTB's proposed assessment should also be cancelled or reduced.

Appellants further assert that the \$10,000 retirement distribution made by Charles Schwab to appellant-wife is a partially nontaxable rollover from a traditional IRA to a Roth IRA. In support, appellants submitted a copy of an amended federal tax return and a federal Form 8606 (Nondeductible IRAs). On the Form 8606, appellants claim \$5,500 as nondeductible contributions to traditional IRAs for 2016 plus \$5,500 in contributions prior to 2016, for a total basis in appellant-wife's traditional IRA of \$11,000. Using those figures, appellants calculated that \$9,966 of the Charles Schwab distribution of \$10,000 was nontaxable, and \$34 was taxable.⁴ FTB replies that it has not received any documentation showing that the distribution was not taxable and invited appellants to provide such evidence.

The basic tax characteristics of a traditional IRA are: (1) deductible contributions; (2) the accrual of tax-free earnings (except with respect to IRC section 511); and (3) the inclusion of distributions in gross income. (See IRC, §§ 219(a), 408(a), (d)(1), (e); see also *Taproot Admin. Servs., Inc. v. Commissioner* (2009) 133 T.C. 202, 206.) Generally, any amount paid or distributed out of a traditional IRA is to be included in gross income when received, as provided under IRC section 72.⁵ (IRC, § 408(d)(1); see also *Repetto v. Commissioner*, T.C. Memo. 2012-

⁴ The Form 8606 is missing information, e.g., line 13 says to add lines 11 and 12 to calculate the nontaxable portion of all of appellants' distributions although line 13 has an entry, lines 11 and 12 are blank. Lines 6 through 10, which are used to compute lines 11 and 12 also are blank. Moreover, it is unclear why appellants claim a basis of \$11,000 in the IRA but find that just \$9,966 is nontaxable.

⁵ California conforms to IRC section 72 pursuant to R&TC section 17085.

168.) Distributions from an IRA are taxable to the extent that they exceed the taxpayer's basis in the IRA. (IRC, § 72(b).) A taxpayer has a zero basis in an IRA unless the taxpayer has made an "investment in the contract." (IRC, §§ 72, 408; Treas. Reg. § 1.408-4(a)(2).) Taxpayers may elect to make nondeductible contributions to an IRA. (IRC, § 408(o).) Nondeductible contributions to an IRA less any prior withdrawals or distributions of nondeductible contributions constitute a taxpayer's investment in the contract. (*Campbell v. Commissioner* (1997) 108 T.C. 54.)

As noted, *ante*, a distribution from a qualified retirement plan is included in income for the year of distribution; however, IRC sections 408(d) and 72(b) provide a general exemption from tax for IRA distributions to the extent that the taxpayer is recovering a basis in the IRA, such as the amount of nondeductible contributions to the IRA account. (IRC, §§ 402(a) & 408(d).)⁶ Appellants assert that most of the Charles Schwab distribution is nontaxable because their basis in appellant-wife's traditional IRA was \$11,000 (\$5,500 in nondeductible contributions during 2016, and \$5,500 in nondeductible contributions in taxable years prior to 2016).⁷

In its opening brief, FTB invited appellants to "provide some documentation that would prove that the IRA distribution of \$10,000.00 was not taxable." On appeal, OTA requested that appellants provide very specific documentation to support their claimed basis and any nondeductible contributions made by appellant-wife during or prior to 2016. Appellants declined to respond to FTB's brief and did not respond to OTA's request for additional briefing. Thus, appellants' assertions with respect to the nontaxability of the \$10,000 distribution to appellant-wife are unsupported and insufficient to carry their burden of proof to show error in FTB's proposed assessment. (See *Appeal of Porreca, supra.*)

Moreover, the documents provided by appellants support the opposite of their contentions. Appellants provided two Forms 5498. The first reports a contribution of \$5,500 in

⁶ The exception differs from the exception for an early distribution as noted on appellant-wife's second Form 1099-R, which indicates that an exception to the early distribution penalty applies; likely, because it was rolled over to another qualified account. (See IRC, § 72(t).) The early distribution penalty was not applied by either the IRS or FTB.

⁷ It is unclear why appellants are treating \$34 of the distribution as taxable when their claimed basis exceeds the amount of the distribution. However, the Form 8606 submitted by appellants was incomplete; for example, \$34 is reported on line 15a of Form 8606, which instructs taxpayers to subtract line 12 from line 7; however, both lines 7 and 12 are blank.

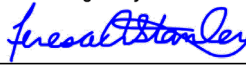
2016, and a distribution of \$5,472 in 2016, which is correctly reported by appellants as a nontaxable distribution. The second Form 5498 corresponds to the \$10,000 distribution and does not show any contributions during 2016. This \$10,000 distribution was reported by Charles Schwab as a taxable transaction. Appellants did not submit any additional information to substantiate other nondeductible contributions to appellant-wife’s traditional IRA during or prior to 2016. Appellants have not shown that FTB erred by including the \$10,000 IRA distribution as taxable income.

HOLDING


Appellants have not established error in FTB’s proposed assessment of additional tax.


DISPOSITION

FTB’s action is sustained.

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Teresa A. Stanley
Administrative Law Judge

We concur:

DocuSigned by:

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Ovsep Akopchikyan
Administrative Law Judge

DocuSigned by:

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Amanda Vassigh
Administrative Law Judge

Date Issued: 8/1/2022