

OFFICE OF TAX APPEALS
STATE OF CALIFORNIA

In the Matter of the Appeal of:
A. BUNYI

) OTA Case No. 21047706
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OPINION

Representing the Parties:

For Appellant: A. Bunyi

For Respondent: Phillip C. Kleam, Tax Counsel III

A. KLETTER, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19045, A. Bunyi (appellant) appeals an action by respondent Franchise Tax Board (FTB) proposing to assess additional tax of \$2,030, and applicable interest, for the 2016 tax year.

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

ISSUE

Whether appellant has shown error in FTB’s proposed assessment of additional tax based on final federal determinations.

FACTUAL FINDINGS

1. Appellant timely filed his 2016 California Resident Income Tax Return on which he claimed an overpayment of \$1,950. After disallowing the dependent exemption of \$344 claimed on the return, FTB refunded appellant \$1,606.
2. Thereafter, FTB received information from the IRS indicating that the IRS had increased appellant’s federal income for the 2016 tax year based on: (1) unreported interest income; (2) income from an early withdrawal (early withdrawal income) from appellant’s

- 403B plan (qualified retirement plan);¹ and (3) a reduction in appellant's itemized deductions on Schedule A based on an increase in the 2 percent miscellaneous deduction threshold. The IRS assessed additional tax on the early withdrawal income (early distribution tax).²
3. FTB issued a Notice of Proposed Assessment (NPA) following the three federal adjustments to appellant's income. FTB also proposed a corresponding early distribution tax on the early withdrawal income. FTB proposed additional tax resulting from its adjustments, which increased appellant's 2016 income by \$4,796.
 4. Appellant protested the NPA, contending that the early withdrawal income from his qualified retirement plan was a loan which was fully repaid and not taxable.
 5. FTB issued a Notice of Action affirming the NPA because appellant provided no evidence that the IRS had canceled or reduced its assessment.
 6. This timely appeal followed.³
 7. On appeal, OTA gave appellant 30 days to submit evidence supporting that the early withdrawal was nontaxable and a loan, and that it was fully repaid. Appellant did not submit any additional evidence in response.

DISCUSSION

A taxpayer shall concede the accuracy of federal changes to the taxpayer's income or state wherein the determination is erroneous. (R&TC, § 18622(a).) It is well settled that a deficiency assessment based on a federal audit report is presumptively correct and that a taxpayer

¹ For the 2016 tax year, R&TC section 17024.5(a)(1) provides that for Personal Income Tax Law purposes, California conforms to the Internal Revenue Code (IRC) as effective on January 1, 2015. Thus, references to the IRC are to the IRC as effective on January 1, 2015. IRC section 72(t)(1) defines a "qualified retirement plan" as one described in IRC sections 401, 403, and 408. (IRC, § 4974(c).) For loan distributions, IRC § 72(p)(4) defines a "qualified employer plan" more narrowly. Appellant transferred funds from a former employer pension plan to appellant's qualified retirement plan. The transfer was reported on a federal Form 1099-R. Subsequently, appellant's qualified retirement plan loaned the funds to appellant. There is no dispute that appellant's 403B plan was a qualified retirement plan under IRC section 4974 or a qualified employer plan under IRC section 72(p)(4).

² IRC section 72(t)(1) provides that if a taxpayer receives an early distribution from a qualified retirement plan, the early withdrawal income is subject to a 10 percent tax, if, among other things, the taxpayer received the distribution before the age of 59½. (IRC, § 72(t)(2)(A)(i).) This tax is in addition to income tax otherwise assessed on the early withdrawal income. (IRC, § 72(p).) R&TC section 17085(c)(1), which conforms to IRC section 72, modifies the early distribution tax to 2.5 percent of the early withdrawal income.

³ On appeal, appellant does not dispute FTB's denial of the dependent exemption, the inclusion of unreported interest income in appellant's California adjusted gross income, or the reduction of his Schedule A deductions. Accordingly, OTA will not address these items further.

bears the burden of proving that the determination is erroneous. (*Appeal of Gorin*, 2020-OTA-018P.) Unsupported assertions are not sufficient to satisfy a taxpayer’s burden of proof. (*Appeal of Bracamonte*, 2021-OTA-156P.)

Gross income shall mean all income from whatever source derived, including interest, dividends, and annuity and pension income, unless the items of income are specifically excluded by law. (Internal Revenue Code (IRC), § 61(a); R&TC, § 17071; Treas. Reg. § 1.61-1(a).) Pursuant to R&TC section 17085(c)(1), which adopts IRC section 72, with modifications,⁴ if a taxpayer receives an early distribution from a qualified retirement plan, the early withdrawal income is subject to the early distribution tax. Loans from qualified employer plans are permitted and not taxable distributions if they comply with the loan rules with respect to amount, duration, and repayment terms. (IRC, § 72(p)(2).) A qualifying loan is required be repaid within five years, except for home loans to a acquire a principal residence. (*Ibid.*) If a loan from a qualified employer plan fails to satisfy the rules and regulations, then it is deemed a taxable distribution. (IRC, § 72(p)(1).)

Appellant’s 2016 IRS wage and income transcript, dated May 13, 2021, indicates that a taxable distribution of \$4,667 was made from appellant’s qualified retirement plan, as reported on Form 1099-R. On appeal, appellant provides retirement savings statements from his former employer pension plan (for the period January 1, 2015, to December 31, 2016) and printouts from appellant’s qualified retirement plan (for the period December 17, 2015, to February 24, 2017) indicating that appellant made withdrawals totaling \$5,000 in November 2016 and made partial “loan repayments” from December 2017 through February 2017. However, the loan does not appear to have been repaid during the period of the account statements provided. Appellant does not provide, nor does the record contain, evidence that the loan was repaid during the statutorily mandated period. Nor did appellant respond to OTA’s additional briefing request that he submit additional evidence supporting that the early withdrawal income was nontaxable, was a loan, and/or was fully repaid. Further, appellant provides no evidence to show that the IRS has cancelled or revised its assessment. Thus, OTA cannot discern whether appellant complied with the rules under IRC section 72(p) such that the purported loan should not be treated as a taxable distribution and should not be subject to the early distribution tax.

⁴ See footnote 2, *supra* [R&TC section 17085(c)(1) reduces the early distribution tax to 2.5 percent from the 10 percent rate imposed under the IRC].

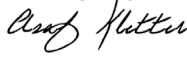
Here, it is unclear whether appellant fully complied with the IRC rules governing repayment of funds borrowed from his qualified retirement plan, and appellant has not shown that the IRS has canceled or revised its assessment. Therefore, appellant failed to show error in FTB’s treatment of the loan from his qualified retirement plan as a taxable distribution in accordance with IRC section 72(p), or in FTB’s proposed assessment of additional tax.

HOLDING

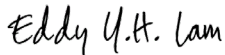
Appellant has not shown error in FTB’s proposed assessment of additional tax based on federal adjustments.


DISPOSITION

FTB’s action is sustained.

DocuSigned by:

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Asaf Kletter
Administrative Law Judge

We concur:

DocuSigned by:

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Eddy Y.H. Lam
Administrative Law Judge

DocuSigned by:

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Teresa A. Stanley
Administrative Law Judge

Date Issued: 11/23/2022