

**OFFICE OF TAX APPEALS  
STATE OF CALIFORNIA**

In the Matter of the Appeal of: ) OTA Case No. 220510309  
C. DEMIR AND )  
A. DEMIR )  
\_\_\_\_\_ )

**OPINION**

Representing the Parties:

For Appellants: C. Demir and A. Demir

For Respondent: Topher Tuttle, Tax Counsel

T. LEUNG, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19045, C. Demir and A. Demir (appellants) appeal an action by Franchise Tax Board (respondent) proposing additional tax of \$1,548, an early distribution tax of \$500, and interest for the 2017 taxable year.

Appellants waived their right to an oral hearing; therefore, this matter is being decided based on the written record.

**ISSUES**

1. Whether appellants’ early withdrawal of \$20,000 from their individual retirement account (IRA) is subject to tax.
2. Whether appellants’ early withdrawal of \$20,000 from their IRA is subject to the 2.5 percent early distribution tax.

**FACTUAL FINDINGS**

1. In 2017, appellants made an early withdrawal of \$20,000 from their IRA and subtracted it as an adjustment to federal adjusted gross income (AGI) on their 2017 California personal income tax return (Form 540).
2. Appellants did not show that the \$20,000 early IRA withdrawal was used to pay for and/or exceeded their 2017 qualified higher education expenses. Appellant C. Demir’s

2017 Form 1098-T, Tuition Statement, reports expenses in the amount of \$2,535, and C. Demir's Forms 1098-T for 2015, 2016, and 2017 report a total amount of expenses of \$13,985. CSU-Long Beach issued all the Forms 1098-T.

3. Respondent issued a Notice of Proposed Assessment (NPA), which added back \$20,000 to appellants' California AGI and imposed the 2.5 percent early distribution tax of \$500, both of which resulted in a greater overall tax liability and denied and/or reduced appellants' renter's credit and personal exemptions. When appellants did not substantiate their payment of qualified higher education expenses for 2017 exceeded the \$20,000 early IRA withdrawal, the NPA was affirmed.

### DISCUSSION

#### Issue 1: Whether appellants' early withdrawal of \$20,000 from their IRA is subject to tax.

Respondent has the initial burden of showing that its action is reasonable and rational. (*Todd v. McColgan* (1949) 89 Cal.App.2d 509, 514; *Appeal of Myers* (2001-SBE-001) 2001 WL 37126924.) Once its burden is satisfied, respondent's determination is presumed to be correct, and the taxpayers have the burden of proving error. (*Todd v. McColgan, supra*, 89 Cal.App.2d at p. 514; *Appeal of Magidow* (82-SBE-274) 1982 WL 11930.) Unsupported assertions are insufficient to satisfy the taxpayers' burden of proof. (*Appeal of Davis*, 2020-OTA-182P.)

Generally, unless an exception applies, a distribution from a qualified retirement plan or an IRA is included in income for the year of distribution. (Internal Revenue Code (IRC), §§ 402(a), 408(d); R&TC, § 17501.) Here, it is undisputed that appellants took a \$20,000 early distribution from their IRA in 2017 and, under these facts, the law provides no applicable exclusion from California AGI for such distributions. Therefore, it was improper for appellants to subtract this \$20,000 from their reported federal AGI.

#### Issue 2: Whether appellants' early withdrawal of \$20,000 from their IRA is subject to the 2.5 percent early distribution tax.

If a taxpayer receives an early distribution from a qualified retirement plan, as described in IRC sections 402 and 408, the early distribution is subject to a 10 percent tax (in addition to the income tax otherwise imposed), if, among other things, the taxpayer received the distribution before the age of 59½. (IRC, §§ 4974(c), 72(t)(1) & (t)(2)(A)(i).) R&TC section 17085(c)(1)

adopts IRC section 72(t) for California tax purposes, but reduces the rate of the early distribution tax from 10 percent to 2.5 percent. There is no reasonable cause exception for the imposition of the 2.5 percent additional tax based on early distributions. (See IRC, § 72.)

The law contains exceptions to the early distribution tax for various kinds of distributions from the many types of retirement plans. For example, an early distribution used by taxpayers to pay for qualified higher education expenses from an IRA is exempt from the early distribution tax under IRC section 72(t)(2)(E). However, in this appeal, appellants did not substantiate that they paid<sup>1</sup> for the expenses reported on their Forms 1098-T. The law provides an exception to the 2.5 percent additional tax only to the extent the \$20,000 early withdrawal did not exceed their qualified higher education expenses (the expenses did) and only if those expenses were paid by them in the year of the early distribution (2017). Since the record has no documentation of whether appellants actually paid for the CSU-Long Beach expenses reported on the 2017 Form 1098-T, no relief from the 2.5 percent early distribution tax is warranted.

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<sup>1</sup> For example, those expenses might have been paid for by C. Demir's employer.

HOLDINGS

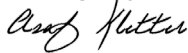
1. Appellants’ early withdrawal of \$20,000 from their IRA is subject to California tax.
2. Appellants’ early withdrawal of \$20,000 from their IRA is subject to the 2.5 percent early distribution tax.


DISPOSITION

Respondent’s action is sustained.

DocuSigned by:  
  
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 Tommy Leung  
 Administrative Law Judge

We concur:

DocuSigned by:  
  
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 Asaf Kletter  
 Administrative Law Judge

DocuSigned by:  
  
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 Cheryl L. Akin  
 Administrative Law Judge

Date Issued: 12/27/2022