

**OFFICE OF TAX APPEALS  
STATE OF CALIFORNIA**

In the Matter of the Appeal of: ) OTA Case Number 22039849  
D. CALLISTER AND )  
T. YOUNG )  
\_\_\_\_\_ )

**OPINION**

Representing the Parties:

For Appellants: Mohit Peter Masih<sup>1</sup>  
Tax Appeals Assistance Program (TAAP)

For Respondent: Parviz Iranpour, Attorney

For Office of Tax Appeals: Tom Hudson, Attorney

T. STANLEY, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19045, D. Callister and T. Young (appellants) appeal an action by respondent Franchise Tax Board (FTB) proposing additional tax of \$2,926<sup>2</sup> and applicable interest for the 2017 taxable year.

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

**ISSUE**

Have appellants shown error in FTB’s calculation of appellants’ Other State Tax Credit (OSTC)?

---

<sup>1</sup> Allan Yue of TAAP submitted appellants’ Supplemental Brief, Connor E. McGettigan of TAAP submitted appellants’ Reply Brief, and appellants submitted the Appeal Letter.

<sup>2</sup> Appellants concede that they have an additional California tax liability of \$1,435 but continue to dispute the \$1,491 remaining amount of FTB’s proposed assessment.

FACTUAL FINDINGS

1. Appellants were residents of Arizona during 2017. Appellant-wife received a Schedule K-1 for her pro-rata share of partnership income, which consisted of income generated in numerous states, including California, and foreign countries.
2. Appellants timely filed their California Nonresident Return (Form 540NR) for the 2017 taxable year reporting total taxable income of \$520,317, California taxable income of \$63,760, and California tax of \$5,279 before credits.
3. Appellants claimed an OSTC of \$3,406 for income taxes that they paid to Arizona in that amount. On Schedule S, Other State Tax Credit, attached to appellants' Form 540NR, appellants reported income taxes paid to Arizona in the amount of \$3,406, double taxed income by California of \$81,230, double taxed income by Arizona of \$653,181 and Arizona adjusted gross income (AGI) of \$576,883. Using the Arizona double taxed income of \$653,181, appellants calculated that they were entitled to a California OSTC equal to 100 percent of the \$3,406 of taxes they paid to Arizona.
4. FTB reviewed appellants' California tax return and issued a Notice of Proposed Assessment (NPA) proposing additional tax of \$2,926, plus applicable interest. FTB determined that appellants incorrectly reported on Schedule S the amount of \$653,181 as income double taxed by both Arizona and California. FTB indicated only the amount of \$81,230 was double taxed by both California and Arizona. The double taxed income of \$81,230 is 14.08 percent of appellants' total Arizona AGI of \$576,883. Thus, FTB reduced appellants' California OSTC to \$480 (14.08 percent of \$3,406 of taxes paid to Arizona).
5. Appellants protested the NPA and submitted to FTB an amended Schedule S which reported \$81,230 as the income double taxed by both Arizona and California and revised the Arizona tax to \$18,582, which is the Arizona total tax amount prior to the application of Arizona tax credits. Based on these revised amounts, appellants claimed a revised California OSTC of \$2,617.
6. On January 28, 2022, FTB issued a Notice of Action, affirming the NPA without modification. This timely appeal followed.
7. On appeal, appellants submit calculations using \$81,230 as the income double taxed by both Arizona and California, income tax paid to Arizona of \$3,406, and Arizona AGI of

\$122,384.<sup>3</sup> Appellants now claim a California OSTC of \$2,261, which leaves the remaining amount in dispute of \$1,491.<sup>4</sup>

### DISCUSSION

Nonresident taxpayers are allowed an OSTC against their “net tax” (as defined in R&TC section 17039) for “net income taxes imposed by and paid to the state of residence” if the following conditions are satisfied: (1) the credit is allowed only if the state of residence either does not tax income of California residents derived from sources within that state or allows California residents a credit against the taxes imposed by that state on such income; (2) the credit is not allowed for taxes paid to a state which allows its residents a credit against taxes imposed by that state for net tax paid or payable under California’s income tax provisions irrespective of whether its residents are allowed a credit against the taxes imposed for income taxes paid to that state; (3) the credit will only be allowed for the portion of the taxes paid to the state of residence as the income taxable under California’s income tax provisions and also subject to tax in the state of residence bears to the entire income upon which the taxes paid to the state of residence are imposed; (4) the credit shall not exceed such proportion of the “net tax” payable to California as the income subject to tax in the state of residence and also taxable by California bears to the taxpayer’s entire taxable income; and, (5) no credit is allowed against California’s tentative minimum tax. (R&TC, § 18002(a)(1)-(5).) However, no credit will be allowed on account of income taxes imposed by another state or country until such taxes are actually paid. (Cal. Code Regs., tit. 18, § 18001-1.)

Tax credits are a matter of legislative grace, and taxpayers bear the burden of proving, by a preponderance of the evidence, entitlement to a claimed tax credit. (*Appeals of Swat-Fame, Inc., et al.*, 2020-OTA-046P; Cal. Code Regs., tit. 18, § 30219(b).) Statutes granting tax credits are strictly construed against taxpayers, and any doubts are resolved in FTB’s favor. (*Appeals of*

---

<sup>3</sup> Appellants calculated the \$122,384 by reducing their total AGI of \$576,833 by \$454,499, which appellants claim is not double taxed by Arizona and other states.

<sup>4</sup> Using Arizona AGI of \$122,384, appellants calculated that 66.37 percent of their income was double taxed by Arizona ( $\$81,230 \div \$122,384 = 66.37$  percent) which they then applied to the Arizona tax of \$3,406. Appellants also offer an alternative formula to calculate the OSTC, using the tax liability owed to Arizona before credits for taxes paid to other states ( $\$3,406 + \$12,196 = \$15,601$ ).

*Swat-Fame, Inc., et al., supra*, citing *Dicon Fiberoptics, Inc. v. Franchise Tax Bd.* (2012) 53 Cal.4th 1227, 1235.)

It is undisputed that appellants are eligible for an OSTC for taxes paid to Arizona.<sup>5</sup> However, the parties dispute the calculation of the OSTC. Appellants argue that their credit against their California “net tax” should have been calculated based on the amount of tax owed to Arizona before application of Arizona’s OSTCs. Appellants assert that FTB’s use of the amount of tax actually paid to Arizona erroneously reduces their California OSTC.

Appellants’ position in this appeal is contrary to the plain language of R&TC section 18002. That section states that the credit is “for net income taxes imposed by and *paid to the state of residence.*” (Italics added.) Appellants must have actually paid the tax to their state of residence, Arizona, in order to qualify for California’s OSTC under R&TC section 18002. (See also Cal. Code Regs., tit. 18, § 18001-1(b).) Paying taxes to other states and jurisdictions might generate a tax credit in Arizona, but those payments cannot be considered payments “to the state of residence,” as required by R&TC section 18002. Instead, those payments to other states and jurisdictions reduce the amount of tax appellants owed to Arizona. (See *Gray v. Franchise Tax Bd.* (1991) 235 Cal.App.3d 36, 40 [a tax credit is a reduction of the amount of tax owed by a taxpayer]; see also FTB Legal Ruling 2017-01.) Furthermore, the OSTC is calculated based on “net income taxes” which is the amount of tax imposed by the other state after the application of that state’s credits, exemptions, and other similar items.<sup>6</sup>

Appellants alternatively argue that the calculation of the OSTC should be based on AGI taxable by Arizona of \$122,384, rather than \$576,883. However, the OSTC is only allowed for the portion of the taxes paid to Arizona as the income taxable under California’s income tax provisions and also subject to tax in Arizona bears to the entire income upon which the taxes paid to Arizona are imposed. (R&TC, § 18002(a)(3).) Thus, the calculation of the OSTC requires the use of the entire AGI taxable by Arizona, which is \$576,883 as reported on appellants’ originally filed Schedule S.

---

<sup>5</sup> See Arizona Revised Statutes §43-1071. As explained in FTB Legal Ruling 2017-01, Arizona provides a credit to California residents for tax paid to California on income sourced to Arizona, so it is a “reverse credit state,” and an Arizona resident is entitled to claim a California OSTC when determining taxes payable to California on California-source income.

<sup>6</sup> Appellants appear to argue that “net income taxes” is defined by R&TC section 17039. Appellants misread R&TC section 18002. The reference to R&TC section 17039 refers to “net tax,” not “net income taxes.” The “net tax” is the amount of California income tax against which taxpayers are allowed to apply the OSTC.

Appellants contend that FTB's calculation is inconsistent with the legislative intent of R&TC section 18002. Appellants argue that this interpretation does not comport with legislative intent to avoid double taxation. However, well-settled principles of statutory construction provide that where the words of the statute are clear and unambiguous, the plain meaning of the language governs. (*Lennane v. Franchise Tax Bd.* (1994) 9 Cal.4th 263, 268). Here, R&TC section 18002 plainly states that the calculation of the OSTC is limited to the amount of tax paid to appellants' state of residence. Moreover, California Code of Regulations, title 18, section 18001-1(b) states that the California OSTC may not be taken until such taxes imposed by another state are actually paid. The Legislature may grant or deny a tax credit in any manner it sees fit, aside from constitutional constraints not at issue here, and the scope, application, and terms of eligibility are entirely for the Legislature to establish. (*Mass v. Franchise Tax Bd.* (2019) 38 Cal.App.5th 959, 965.) Appellants have not shown that the Legislature intended for tax credits (such as an OSTC provided by the state of residence) to count as payment of tax to the state of residence. Moreover, Arizona has already credited appellants for the taxes paid to other states on \$454,499 of appellants' Arizona AGI. Appellants have not explained how this equates to California double taxing their income.


The parties do not dispute that appellants paid \$3,406 in taxes to Arizona. Therefore, that is the proper amount to use for calculating the OSTC. (See *Appeal of Fessler* (81-SBE-048) 1981 WL 11776.) Additionally, appellants have not met their burden to show that their Arizona AGI, which was used in FTB's computation, was incorrect; thus, appellants have not shown error in FTB's calculation of the OSTC.

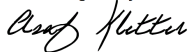
HOLDING


Appellants have not shown error in FTB’s calculation of appellants’ OSTC.

DISPOSITION

FTB’s proposed assessment is sustained.

DocuSigned by:  
  
0CC6C6ACCC6A44D...  
\_\_\_\_\_  
Teresa A. Stanley  
Administrative Law Judge

We concur:  
DocuSigned by:  
  
D17AEDDCAAB045B...  
\_\_\_\_\_  
Asaf Kletter  
Administrative Law Judge

DocuSigned by:  
  
A11783ADD49442B...  
\_\_\_\_\_  
Huy “Mike” Le  
Administrative Law Judge

Date Issued: 12/20/2023