

- \$3,855 and a self-assessed estimated tax penalty of \$31, resulting in an overpayment of \$1,262.
2. FTB accepted appellants' 2014 return as filed and refunded the claimed overpayment of \$1,262.
 3. The IRS audited appellants' 2014 Form 1040 and made the following relevant adjustments to their AGI: disallowing Schedule C (other) expenses of \$41,412, travel expenses of \$17,240, and car and truck expenses of \$18,643; disallowing a student loan interest deduction of \$226; disallowing a capital loss deduction of \$1,431; and allowing a self-employed AGI adjustment of \$2,212. These adjustments collectively increased appellants' federal AGI by \$76,740, which increased their federal taxable income to \$144,644. The IRS assessed additional tax of \$23,667 and imposed an accuracy-related penalty of \$4,733.40, plus applicable interest.¹
 4. Appellants protested the IRS assessment and brought the case before the U.S. Tax Court. On December 18, 2018, the U.S. Tax Court entered a decision affirming the IRS assessment after appellants had approximately 10 months to resolve the case with the IRS and failed to appear at the court's trial session or present evidence to the court.
 5. FTB received a copy of the federal adjustment from the IRS. To the extent applicable under California law, FTB made corresponding adjustments to appellants' 2014 California tax return.
 6. FTB issued appellants a Notice of Proposed Assessment (NPA) making the same adjustments as the IRS. As a result, appellants' California taxable income increased by \$76,740 to \$165,502. FTB proposed additional tax of \$6,965 and imposed an accuracy-related penalty of \$1,393, plus interest.²
 7. Appellants protested the NPA and provided attachments relating to the 2011 tax year. FTB issued a letter in response to appellants stating that the NPA is based on the federal adjustment made following the U.S. Tax Court decision. FTB requested that appellants provide documentation indicating that the IRS made changes to the 2014 federal determination as stated in appellants' protest letter within 30 days.

¹ The federal accuracy-related penalty is 20 percent of the assessed additional tax.

² The California accuracy-related penalty is 20 percent of the proposed additional tax.

8. After appellants failed to respond to its letter, FTB issued a Notice of Action affirming the NPA.
9. Appellants filed this timely appeal.

DISCUSSION

Issue 1: Whether appellants have established error in FTB's proposed assessment for the 2014 tax year, which is based on a final federal determination.

R&TC section 18622(a) provides that the taxpayer shall either concede the accuracy of a federal determination or state where it is erroneous. It is well settled that FTB's proposed assessment based on a federal determination is presumptively correct and the taxpayer bears the burden of proving that the determination is erroneous. (*Todd v. McColgan* (1949) 89 Cal.App.2d 509, 514; *Appeal of Valenti*, 2021-OTA-093P.) Unsupported assertions are insufficient to satisfy a taxpayer's burden of proof. (*Appeal of Gorin*, 2020-OTA-018P.) In the absence of credible, competent, and relevant evidence showing that FTB's proposed assessment is incorrect, it must be sustained. (*Appeal of Valenti, supra.*)

Income tax deductions are a matter of legislative grace, and a taxpayer who claims a deduction has the burden of proving by competent evidence that he or she is entitled to that deduction or credit. (*New Colonial Ice Co. v. Helvering* (1934) 292 U.S. 435, 440; *Appeal of Vardell*, 2020-OTA-190P.) To meet that burden, a taxpayer must point to an applicable statute and show by credible evidence that the transactions in question come within its terms. (*Appeal of Jindal*, 2019-OTA-372P.) FTB's denial of a claimed deduction is presumed correct until the taxpayer has proven his or her entitlement. (*Appeal of Janke* (80-SBE-059) 1980 WL 4988.)

Appellants contend that they provided additional information to FTB and requested a phone call to discuss their case. However, appellants do not provide copies of any information purportedly provided to FTB. FTB has provided appellants' protest letter and attachments, which do not pertain to the year at issue. Additionally, appellants were granted an extension to file a reply brief in this appeal but did not do so, and appellants did not reply to OTA's letter asking if appellants would like an oral hearing. In sum, appellants have had opportunities to provide additional argument and evidence but have failed to do so.

FTB's proposed assessment of additional tax is based on adjustments made to appellants' federal income as a result of an IRS exam, affirmed by a decision of the U.S. Tax Court, and is

reflected in appellants' federal transcript. The record does not show that the federal adjustments have been modified, altered, withdrawn, cancelled, or rescinded. Accordingly, appellants have not established error in FTB's determination.

Issue 2: Whether appellants have established a basis to abate the accuracy-related penalty.

R&TC section 19164 generally incorporates the provisions of Internal Revenue Code (IRC) sections 6662 and 6664 and, as relevant here, imposes an accuracy-related penalty of 20 percent on any portion of the underpayment attributable to a substantial understatement of income tax. (IRC, § 6662(b)(2).) An "understatement" of tax is defined as the excess of the amount of tax required to be shown on the return for the tax year, over the amount of tax imposed that is shown on the return, reduced by any rebate. (IRC, § 6662(d)(2)(A)(i)-(ii).) For individual taxpayers, the understatement of income tax is substantial if it exceeds the greater of 10 percent of the tax required to be shown on the return, or \$5,000. (IRC, § 6662(d)(1)(A)(i)-(ii).)

The taxpayer bears the burden of proving any defenses to the imposition of the accuracy-related penalty. (*Recovery Group, Inc. v. Commissioner*, T.C. Memo. 2010-76, affd. (1st Cir. 2011) 652 F.3d 122.) In determining whether there is a substantial understatement, the amount of the understatement shall be reduced by any portion of the understatement that is attributable to: (1) the tax treatment of any item by the taxpayer if there is or was substantial authority for such treatment; or (2) any item if the relevant facts affecting the item's tax treatment were adequately disclosed in the return (or in a statement attached to the return) and there is a reasonable basis for the tax treatment of the item by the taxpayer. (IRC, § 6662(d)(2)(B)(i)-(ii); see also Treas. Reg. § 1.6662-4(d)-(f).) IRC section 6664(c)(1) also provides that the accuracy-related penalty shall not be imposed under IRC section 6662 "with respect to any portion of an underpayment if it is shown that there was a reasonable cause for such portion and that the taxpayer acted in good faith with respect to such portion."

FTB imposed a 20 percent accuracy-related penalty based on a substantial understatement of tax. Appellants' understatement is considered substantial if it exceeds the greater of 10 percent of the tax required to be shown on the return, or \$5,000. (IRC, § 6662(d)(1)(A).) Here, \$5,000 is greater than 10 percent of the amount of tax required to be

shown on appellants’ 2014 return.³ Appellants’ understatement of California income tax of \$6,965 is substantial because it exceeds \$5,000. FTB thus properly imposed the accuracy-related penalty because there was a substantial understatement of tax.

Appellants do not contend, and the evidence does not show, that any portion of the understatement is attributable to: (1) appellants’ tax treatment of an item for which there is or was substantial authority for such treatment; or (2) any item for which the relevant facts affecting the item’s tax treatment were adequately disclosed in appellants’ return (or in a statement attached to the return) and there is a reasonable basis for appellants’ tax treatment of the item. (IRC, § 6662(d)(2)(B).) Appellants have not met their burden of proving any defense to the imposition of the accuracy-related penalty. Accordingly, appellants have not established a basis to abate the penalty.

HOLDINGS

1. Appellants have not established error in FTB’s proposed assessment for the 2014 tax year, which is based on a final federal determination.
2. Appellants have not established a basis to abate the accuracy-related penalty.

DISPOSITION


FTB’s action is sustained.

DocuSigned by:

 32D46B0C49C949F...

 Veronica I. Long
 Administrative Law Judge

We concur:

DocuSigned by:

 3AF5C32BB93B450...

 Kenneth Gast
 Administrative Law Judge

DocuSigned by:

 1EAB8BDA3324477...

 Eddy Y.H. Lam
 Administrative Law Judge

Date Issued: 3/8/2024

³ The total tax required to be shown on appellants’ 2014 return is \$9,527. Ten percent of this amount is \$952.70.