

**OFFICE OF TAX APPEALS
STATE OF CALIFORNIA**

In the Matter of the Appeal of:)
A. MATHARU AND) OTA Case No. 22029706
J. MATHARU)
_____)

OPINION

Representing the Parties:

For Appellants: A. Matharu
J. Matharu
For Respondent: Bradley J. Coutinho, Attorney Supervisor

A. KLETTER, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19045, A. Matharu and J. Matharu (appellants) appeal an action by respondent Franchise Tax Board (FTB) proposing additional tax of \$11,606, an accuracy-related penalty (ARP) of \$2,321.20, and applicable interest for the 2014 tax year.

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

ISSUES

1. Whether appellants have shown error in FTB’s proposed assessment of additional tax, which is based on a final federal determination.
2. Whether the ARP was properly imposed, and if so, whether it may be abated.
3. Whether appellants are entitled to interest abatement.

FACTUAL FINDINGS

1. Appellants timely filed their joint California Resident Income Tax Return (Form 540) for the 2014 tax year.
2. FTB received information from the IRS that it had audited appellants’ 2014 tax year and, as relevant here, increased their capital gain income by \$135,266, increased their

Schedule E losses by \$10,778, and disallowed \$306 of their student loan interest. The IRS's adjustments increased appellants' taxable income by a total of \$124,794 (\$135,266 - \$10,778 + \$306). The IRS determined that appellants' revised taxable income was \$189,968, assessed additional tax based on its adjustments, and imposed a federal ARP. On April 15, 2019, the IRS's determination became a final federal determination for the 2014 tax year. Appellants did not report the federal changes to FTB.

3. On November 30, 2020, FTB issued appellants a Notice of Proposed Assessment (NPA) that followed the IRS adjustments, as applicable under California law, and proposed to increase appellants' 2014 California taxable income by \$124,794. The NPA determined total tax of \$15,891, and proposed to assess additional tax of \$11,606, an ARP of \$2,321.20, and applicable interest.
4. Appellants timely protested the NPA. FTB acknowledged the protest and proposed to affirm its position in a letter dated October 26, 2021. The October 26, 2021 letter explained that FTB's adjustments were based on the final federal determination, and that appellants did not provide documentation showing that the IRS adjustments were reduced or cancelled, or that the federal ARP was cancelled or reduced.
5. Appellants did not reply, and on January 12, 2022, FTB issued a Notice of Action affirming the NPA for the 2014 tax year.
6. Appellants timely filed this appeal.
7. On appeal, FTB provides appellants' 2014 federal account transcript dated May 10, 2023, which shows that as of that date, the IRS had not cancelled or reduced its assessment of tax and had not reduced or abated the federal ARP.

DISCUSSION

Issue 1: Whether appellants have shown error in FTB's proposed assessment of additional tax, which is based on a final federal determination.

When the IRS makes a final federal determination, a taxpayer must concede the accuracy of the federal changes to a taxpayer's income or state where the changes are erroneous. (R&TC, § 18622(a).) It is well settled that a deficiency assessment based on a federal adjustment to income is presumed to be correct and a taxpayer bears the burden of proving that FTB's

determination is erroneous. (*Todd v. McColgan* (1949) 89 Cal.App.2d 509, 514; *Appeal of Valenti*, 2021-OTA-093P.)

Here, FTB received information from the IRS that appellants' federal taxable income was increased for the 2014 tax year. Therefore, FTB's corresponding adjustments are presumptively correct. (*Todd v. McColgan, supra*; *Appeal of Valenti, supra*.) Appellants do not contest the student loan interest deduction or Schedule E loss adjustments. Thus, OTA concludes that FTB's adjustments based on these two federal adjustments are correct.

Appellants contest the capital gain adjustment. On appeal, FTB provides appellants' 2014 federal account transcript, which shows that as of May 10, 2023, the IRS had not cancelled or reduced its assessment of tax. On appeal, appellants argue that the IRS made an error in adjusting their cost basis in an S corporation they owned, which resulted in the IRS's erroneous determination of their capital gain. Appellants also assert that they filed an appeal to adjust their cost basis with the IRS. However, appellants have not provided any documentation to support these assertions or substantiate the proper capital gain computation, which they assert should equal zero. Unsupported assertions are insufficient to satisfy a taxpayer's burden of proof with respect to an assessment based on federal action. (*Appeal of Dillahunty*, 2024-OTA-024P.) In the absence of credible, competent, and relevant evidence showing error in FTB's proposed assessment, or in the federal determination on which FTB's proposed assessment was based, it must be upheld. (*Appeal of Valenti, supra*; *Appeal of Dillahunty, supra*.)

Issue 2: Whether the ARP was properly imposed, and if so, whether it may be abated.

R&TC section 19164, which generally incorporates the provisions of Internal Revenue Code (IRC) section 6662,¹ provides for an ARP of 20 percent of the portion of an underpayment of the tax that was required to be shown on the taxpayer's return. (See *Appeal of Daneshgar*, 2021-OTA-210P.) When FTB imposes a penalty, such as an ARP, it is presumed to have been imposed correctly. (*Appeal of Steffier*, 2024-OTA-017P.) As relevant here, the penalty applies to the portion of the underpayment attributable to any 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 tax return for the tax year, over the amount of tax that is shown on

¹ For the 2014 tax year, R&TC section 17024.5(a)(1)(O) provides that for Personal Income Tax Law purposes, California conforms to the IRC as of a specified date of January 1, 2009. Thus, references to the IRC contained in this Opinion are to the IRC as in effect on January 1, 2009.

the return, reduced by any rebate. (IRC, § 6662(d)(2)(A)(i)-(ii).) For individual taxpayers, there is a “substantial understatement of income tax” when the amount of the understatement for a tax year 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, the record shows that FTB’s imposition of the ARP was proper for the 2014 tax year. The tax required to be shown on the Form 540 was \$15,891. FTB determined that the additional tax, or understated tax, was \$11,606. The understated tax of \$11,606 exceeds \$5,000, which is greater than 10 percent of tax required to be shown on the Form 540 of \$1,589.10 (\$15,891 x 10 percent), and therefore it was a substantial understatement. FTB thus correctly calculated and imposed the ARP.

There are various exceptions to the imposition of the ARP. The ARP shall be reduced by the portion of the understatement attributable to the tax treatment of any item if there is or was substantial authority for that treatment, or the relevant facts affecting the item’s tax treatment are adequately disclosed and there is a reasonable basis for the tax treatment of such item. (IRC, § 6662(d)(2)(B)(i-ii).) Additionally, the ARP will not be imposed to the extent that a taxpayer has shown that a portion of the underpayment was due to reasonable cause and the taxpayer acted in good faith with respect to that portion of the underpayment. (IRC, § 6664(c)(1); Treas. Reg. §§ 1.6664-1(b)(2), 1.6664-4(a).) 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.)

Appellants have not asserted any facts or legal authority to establish any applicable exceptions to the ARP, and the record does not reflect any potential grounds for abating it. Therefore, the ARP cannot be abated.

Issue 3: Whether appellants are entitled to interest abatement.

Interest must be assessed from the date a tax payment is due through the date that it is paid. (R&TC, § 19101(a).) Imposing interest is mandatory; it is not a penalty, but it is compensation for the taxpayer’s use of money after it should have been paid to the state. (*Appeal of Moy*, 2019-OTA-057P.) Generally, to obtain relief from interest, a taxpayer must

qualify under R&TC section 19104 or 21012.² Pursuant to R&TC section 19104, FTB is authorized to abate or refund interest if there has been an unreasonable error or delay in the performance of a ministerial or managerial act by an employee of respondent. Pursuant to R&TC section 21012, a taxpayer may be relieved of interest based on reasonable reliance on written advice from FTB.

Appellants do not allege that either of these two statutory provisions for interest abatement apply to the facts of this case, and OTA concludes based on the evidence in the record that no statutory provision for abatement applies. Therefore, there is no basis to abate interest.


² Under R&TC section 19112, FTB may waive interest for any period for which it determines that an individual or fiduciary is unable to pay interest due to extreme financial hardship. OTA does not have authority to review FTB's denial of a request to waive interest under R&TC section 19112. (*Appeal of Moy, supra.*)

HOLDINGS

1. Appellants have not shown error in FTB’s proposed assessment of additional tax, which is based on a final federal determination.
2. The ARP was properly imposed and it may not be abated.
3. Appellants are not entitled to interest abatement.

DISPOSITION

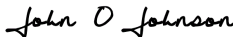
FTB’s action is sustained.

DocuSigned by:

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 Asaf Kletter
 Administrative Law Judge

We concur:

DocuSigned by:

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 Kenneth Gast
 Administrative Law Judge

DocuSigned by:

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 John O. Johnson
 Administrative Law Judge

Date Issued: 6/12/2024