



whereas they excluded the 401(k) contributions from their federal taxable income and did not pay federal tax on their 401(k) contributions for federal income tax purposes.

2. After appellants moved to California, they received \$75,000 of distributions from their 401(k) in 2017.
3. Appellants filed a 2017 California Resident Income Tax Return (Form 540). On Schedule CA (540), California Adjustments – Residents, appellants subtracted \$75,000 from their California adjusted gross income (AGI) for distributions they received from their 401(k).
4. On June 29, 2021, FTB issued a Notice of Proposed Assessment (NPA), which increased appellants' reported 2017 California taxable income by \$75,000 due to their 401(k) distributions of \$75,000. The NPA proposed additional tax of \$3,077, plus interest from April 15, 2018, to April 15, 2021.
5. Appellants protested the NPA and asserted that they had paid tax on their 401(k) contributions to Pennsylvania in the years when they made contributions to their 401(k). At FTB's request, appellants provided FTB with documentation showing that they paid taxes of \$2,303 to Pennsylvania from 2010 through 2013 when they made contributions to their 401(k) and a completed 2017 Schedule S claiming an other state tax credit (OSTC) of \$2,303 for taxes paid to Pennsylvania.
6. On July 26, 2021, appellants made a payment of \$3,554.90 to FTB.
7. On December 28, 2022, FTB issued a Notice of Action (NOA) revising its proposed assessment of tax from \$3,077 to \$774. The NOA allowed appellants' OSTC of \$2,303 for taxes paid to Pennsylvania from 2010 through 2013 based on the 2017 Schedule S that appellants submitted with their protest.
8. The NOA included interest from April 15, 2018, through April 15, 2021, and interest from July 14, 2021, through December 28, 2022. The NOA stated that FTB received appellants' payment of \$3,554.90 on July 26, 2021, and that while interest computation in the NOA did not yet reflect the payment, a revised billing notice would be issued and interest would only be charged until the date the payment was received.
9. This timely appeal follows.

## DISCUSSION

### Burden of Proof

Tax credits are a matter of legislative grace, and taxpayers bear the burden of proving they are entitled to claimed credits. (*Appeal of Buehler*, 2023-OTA-215P.) Unsupported assertions are not sufficient to satisfy a taxpayer’s burden of proof. (*Appeal of Morosky*, 2019-OTA-312P.) In the absence of credible, competent, and relevant evidence showing error in FTB’s determination, FTB’s determination must be upheld. (*Ibid.*) A taxpayer’s failure to produce evidence that is within his or her control gives rise to a presumption that such evidence, if provided, would be unfavorable to the taxpayer’s case. (*Ibid.*)

### California’s Personal Income Tax Law

California imposes a tax on a California resident’s entire taxable income. (R&TC, § 17041(a)(1).) R&TC section 17071 incorporates Internal Revenue Code (IRC) section 61, which defines “gross income” as “all income from whatever source derived,” including pension income. Generally, a distribution from a qualified retirement plan or an individual retirement account is included in income for the year of distribution. (IRC, §§ 402(a), 408(d)(1).)<sup>1</sup>

### OSTC

R&TC section 18001(a)(1) provides a tax credit to California residents for taxes paid to another state on income derived from sources within that other state. Provided statutory requirements are met, the OSTC is available to California residents against their California net tax for net income taxes imposed by and paid to another state. (*Ibid.*) Since income is generally included in taxable income in the year of receipt (IRC, § 451)<sup>2</sup>, income that is subject to double taxation is most often taxed by both states in the same tax year. However, when the double-taxed income is subject to taxation by California and another state in a different tax year,

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<sup>1</sup> California generally conforms to IRC sections 402(a) and 408(d), with modifications not relevant to this appeal. (R&TC, §§ 17501(a), 17504, 17507.)

<sup>2</sup> California generally conforms to IRC section 451 with modifications not relevant to this appeal. (R&TC, § 17551.)

California Code of Regulations, title 18, § 18001-1(b) provides that the OSTC “may be taken either at the time of filing returns under the law or subsequently[.]”<sup>3</sup>

### Analysis

It is undisputed that appellants received 401(k) distributions of \$75,000 during 2017 while they were California residents and they previously paid Pennsylvania taxes on their 401(k) contributions while they were Pennsylvania residents. Appellants assert that: (1) the 401(k) distributions should not be included in their California taxable income for 2017; (2) the Schedule S should not apply; and (3) the NOA charged interest incorrectly.

In their first point, appellants assert that the 401(k) distributions should not be included in California taxable income in 2017, because they paid Pennsylvania tax on their 401(k) contributions. Appellants acknowledge that the 401(k) distributions are includable in their federal taxable income for 2017, because they did not pay federal taxes on their 401(k) contributions. Appellants’ perspective is understandable, but it does not reflect California income tax law. California law provides that 401(k) distributions are included in taxable income in the year of distribution. (IRC, §§ 402(a), 408(d)(1); R&TC, §§ 17501(a), 17504, 17507.) California law does not include a provision to exclude 401(k) distributions where tax has already been paid to another state. The only recourse available to taxpayers in this circumstance is to file Schedule S and claim the OSTC.

Appellants next assert that Schedule S does not accommodate their circumstances. FTB does not dispute that Schedule S is not generally intended for claiming the OSTC for a different tax year than that in which the tax was paid to the other state. Schedule S computes two amounts: (1) the ratio of double-taxed income to California AGI, multiplied by the taxpayer’s California tax liability; and (2) the ratio of double-taxed income to the other state AGI, multiplied by the taxpayer’s other state tax liability. Schedule S computes the OSTC as the lesser of these two amounts. When the double-taxed income is subject to taxation by California

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<sup>3</sup> R&TC section 19311.5 provides that, for taxes paid to another state on or after January 1, 2009, the credit available under R&TC section 18001 must be claimed by the later of: (1) one year from the date the tax is paid to the other state, or (2) the time period provided in R&TC section 19306. R&TC section 19306 provides that no credit may be allowed after a period ending: (1) four years from the date the return was filed, if the return was timely filed pursuant to an extension of time to file; (2) four years from the date the return was due, determined without regard to any extension of time to file; or (3) one year from the date of overpayment.

and another state in different tax years, this computation can become distorted and particularly complicated.

Even in the usual case of taxpayers claiming OSTC for the same tax year, the OSTC will only allow taxpayers the lesser of the amount of their California tax liability attributable to the double-taxed income, or their other state tax liability attributable to the double-taxed income. The amount of OSTC is not based solely on the amount of double-taxed income, but on the *ratio* of tax liability attributable to that income. For this reason, taxpayers often have some amount of remaining tax liability even after full application of the OSTC because the amount of their tax liability paid to the other state that is attributable to double-taxed income is taxed at a lower rate than California.<sup>4</sup>

FTB allowed appellants the full amount of OSTC claimed by them on Schedule S. In addition, appellants have not provided documentation supporting that they paid more than \$2,303 in income tax to Pennsylvania on the 401(k) contributions. Accordingly, appellants have not demonstrated entitlement to additional OSTC.

Last, appellants assert that the NOA included a proposed assessment of interest after they had already paid the tax liability in full. While the NOA does include interest after appellants' July 26, 2021 payment date, it also confirms that FTB received appellants' payment and states that interest will be charged only until the date payment was received and that appellants will receive a revised billing notice. Both parties are in agreement that appellants will not be charged interest after appellants' July 26, 2021 payment date.

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<sup>4</sup> Regarding appellants' assertion that subjecting them to double taxation is unconstitutional, California Code of Regulations, title 18, section 30104 states that OTA does not have jurisdiction to consider whether a California statute is invalid or unenforceable under the California or U.S. Constitutions, unless a federal or California appellant court has already made such a determination. Further, Article III, section 3.5 of the California Constitution prohibits OTA from declaring a statute to be unconstitutional or refusing to enforce it on the basis that it is unconstitutional unless an appellate court has already determined that such a statute is unconstitutional. (*Appeal of Porreca*, 2018-OTA-095P.) Appellants cite no federal or California appellate court ruling that determined R&TC section 18001, which sets forth the OSTC, is invalid or unenforceable, and OTA finds no such authority. (Cal. Const., Art. III, § 3.5.)

HOLDING

Appellants have not shown error in the proposed assessment for the 2017 tax year.

DISPOSITION

FTB's action is sustained.

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*Veronica I. Long*  
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Veronica I. Long  
Administrative Law Judge

Date Issued: 5/21/2024