

4. This timely appeal followed. On appeal, appellant provides a federal Schedule C for the 2018 tax year, showing appellant claiming \$162,470 in business expenses and deductions.

DISCUSSION

R&TC section 18622(a) provides that a taxpayer must either concede the accuracy of a final federal determination or state wherein it is erroneous. A deficiency assessment based on federal adjustments to income is presumptively correct and the taxpayer bears the burden of proving that the determination is erroneous. (*Appeal of Dillahunty*, 2024-OTA-024P.)

Unsupported assertions are not sufficient to satisfy a taxpayer's burden of proof with respect to a deficiency assessment based on a federal action. (*Ibid.*)

In this appeal, based on the final federal determination, FTB proposed to assess additional taxes, plus interest. Although FTB may base its proposed assessment on a final federal determination to the extent applicable under California law, it is not bound to do so and can conduct an independent investigation. (See Cal. Code Regs., tit. 18, § 19059(d); see also *Appeal of Black*, 2023-OTA-023P.) A taxpayer bears the burden to establish FTB's proposed assessment based on a final federal determination is incorrect. (*Appeal of Black*, *supra*.) However, in the absence of credible, competent, and relevant evidence showing FTB's determination is incorrect, it must be upheld. (*Ibid.*)

Appellant's 2018 IRS Account Transcript shows that the IRS did not reduce or cancel the federal assessment. Appellant does not dispute earning gross receipts or sales of \$161,220 in 2018; rather, appellant claims that he did not make any money and instead had a net loss in 2018. On appeal, appellant submits a federal Schedule C indicating he is entitled to business expenses and deductions in the amount of \$162,470. 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. (*Appeal of Vardell*, 2020-OTA-190P.) To sustain his or her burden of proof, a taxpayer must be able to point to an applicable deduction statute and show that he or she came within its terms. (*Appeal of Dandridge*, 2019-OTA-458P.)

Concerning business expenses, California law incorporates Internal Revenue Code (IRC) section 162(a), except as otherwise provided. (R&TC, § 17201.) IRC section 162(a) authorizes a deduction for "all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business" (*Ibid.*; see also *Roberts v. Commissioner*, T.C. Memo. 2012-197 (*Roberts*)). The expenses must be both ordinary and

necessary business expenditures directly related to the taxpayer's trade or business. (*Deputy v. du Pont* (1940) 308 U.S. 488, 494, 497; Treas. Reg. § 1.162-1(a).) A taxpayer has the burden of showing that a particular expense is not a personal, living, or family expense. (*Heineman v. Commissioner* (1984) 82 T.C. 538, 542.) A taxpayer is required to keep books and records sufficient to enable FTB to determine a taxpayer's correct tax liability. (*Higbee v. Commissioner* (2001) 116 T.C. 438, 440.)

R&TC section 17201 also incorporates IRC section 274(d). For the 2018 tax year, California law conformed to the 2015 version of the IRC. (R&TC section 17024.5(a)(1)(P).) IRC section 274(d) prohibits an IRC section 162 deduction for the following types of expenses, unless they were substantiated by adequate records or sufficient corroborating evidence: (1) any travel expense, including meals and lodging away from home; (2) any item with respect to an activity in the nature of entertainment, amusement, or recreation; (3) an expense for gifts; or (4) the use of "listed property," as defined in IRC section 280F(d)(4), which includes passenger vehicles. (IRC, § 274(d); see also *Roberts, supra*.) The substantiation requirements for compliance with IRC section 274 are stricter than those required for other kinds of deductions, particularly the deduction for ordinary and necessary business expenses found in IRC section 162. (*D.A. Foster Trenching Co., Inc. v. U.S.* (Ct. Cl. 1973) 473 F.2d 1398, 1401.) The tax court held that documents like receipts are generally sufficient proof of an expenditure as long as there is sufficient information to identify the amount, date, place and character of the transaction; however, "[r]eceipts often fail as proof because they do [not] show any particular business purpose." (*H&M, Inc. v. Commissioner*, T.C. Memo. 2012-290, fn. 17.)

Here, appellant has not substantiated any of the deductions claimed on federal Schedule C with supporting documentation. For expenses with heightened substantiation requirements, appellant fails to provide receipts or invoices establishing the date, specific location, and business purpose for the expense, as required by R&TC section 17201.

HOLDING

Appellant has not shown error in FTB’s proposed assessment based on a federal assessment for the 2018 tax year.

DISPOSITION

FTB’s action is sustained.

DocuSigned by:
Sara A. Hosey
6D3FE4A0CA514E7...
Sara A. Hosey
Administrative Law Judge

We concur:

DocuSigned by:
Asaf Kletter
D17AEDDCAAB045B
Asaf Kletter
Administrative Law Judge

Signed by:
Natasha Ralston
25F8FF08FF56478...
Natasha Ralston
Administrative Law Judge

Date Issued: 3/19/2025