

3. FTB followed the federal adjustments and issued appellant a Notice of Proposed Assessment (NPA) which proposed to disallow the Schedule A deductions of \$24,962, resulting in additional tax of \$2,277, plus interest.
4. Appellant protested the proposed assessment, and FTB issued appellant a Notice of Action affirming the NPA.
5. This timely appeal followed.
6. On appeal, FTB submits federal Form 4549, Report of Income Tax Examination Changes (Form 4549), which shows the IRS adjusted appellant's Schedule A deductions or expenses because appellant failed to provide her employer reimbursement policy and necessary verification showing the claimed expenses were ordinary and necessary for appellant's business.

DISCUSSION

R&TC section 18622(a) provides that a taxpayer shall either concede the accuracy of a federal determination or state where it is erroneous. It is well settled that a deficiency assessment based on a federal adjustment is presumptively correct, and the taxpayer bears the burden of proving that FTB's determination is erroneous. (*Appeal of Gorin*, 2020-OTA-018P.) Unsupported assertions are insufficient to satisfy a taxpayer's burden of proof with respect to an assessment based on a federal action. (*Ibid.*)

Income tax deductions are a matter of legislative grace, and a taxpayer bears the burden of establishing entitlement to the deductions claimed. (*Appeal of Dillahunty*, 2024-OTA-024P.) To meet this burden, a taxpayer must point to an applicable statute authorizing the deduction and show by credible evidence that the deduction claimed falls within the scope of the statute. (*Ibid.*) R&TC section 17201, which generally incorporates Internal Revenue Code (IRC) sections 162, 262, 274, and 280F into California law, provides a deduction for unreimbursed ordinary and necessary expenses paid during the taxable year in carrying on a trade or business. A trade or business expense is ordinary for purposes of IRC section 162 if it is normal or customary within a particular trade, business, or industry, and is necessary if it is appropriate and helpful for the development of the business. (*Roberts v. Commissioner*, T.C. Memo. 2012-197.) Courts have held that an expense is not necessary if an employee fails to claim reimbursement for the expenses incurred in the course of employment, when entitled to do so. (*Orvis v. Commissioner* (9th Cir. 1986) 788 F.2d 1406,1408.) In general, no deductions shall be allowed for personal, living, or family expenses. (IRC, § 262(a).)

IRC section 274(d) imposes heightened substantiation requirements for certain types of expenses, including: (1) travel expenses, such as meals and lodging away from home; (2) entertainment; (3) gifts; or (4) any listed property,¹ which includes passenger automobiles. To deduct such expenses, a taxpayer must substantiate by adequate records or sufficient evidence to corroborate the taxpayer's own statement: (1) the amount of the expense or other item; (2) the time and place of the travel or entertainment or the date and description of the gift; (3) the business purpose of the expense or other item; and (4) the business relationship to the taxpayer of the person receiving the benefit. (IRC, § 274(d).)

Here, the evidence shows that the IRS disallowed appellant's claimed expenses and deductions of \$24,962. FTB made corresponding adjustments, as detailed in the NPA, which are the subject of this appeal. Appellant must show that either the IRS reduced or cancelled appellant's disallowed expenses and deductions, or that, regardless of the federal action, appellant is entitled to the disallowed amounts.

On appeal, appellant states that she is still appealing the IRS determination and that she is providing worksheets and bank statements to support the amounts claimed on the return. Appellant disagrees with FTB's decision to propose additional taxes and asserts that the decision does not reflect the expenses substantiated by third-party records. In support, appellant provides copies of bank and credit card statements for the 2017 taxable year, donation receipts, and ledgers detailing appellant's Schedule A medical expenses, other taxes, charitable contributions, job expenses and miscellaneous deductions.²

As to appellant's ongoing appeal with the IRS, the record shows that, as of March 18, 2024, there was no change in the federal disallowance of claimed expenses and deductions or in the additional federal tax assessed. On the contrary, appellant's federal Account Transcript shows that the IRS resolved appellant's claim on May 1, 2023, with no changes made to the additional tax liability. Lastly, as noted by FTB, an IRS Examiner explained that the IRS disallowed itemized deductions of \$24,962 because appellant failed to provide an employer reimbursement policy and the necessary verification for the vehicle and travel expenses claimed on Schedule A to support the bank and credit card statements appellant provided. The IRS acknowledged appellant's correspondence dated January 7, 2020, and indicated that the IRS continued to disallow appellant's expenses and deductions because appellant "did not establish that the business expense shown on [her] tax return was paid or

¹ As defined in IRC section 280F(d)(4).

² The IRS made no adjustments to appellant's claimed medical expenses and charitable contributions.

incurred during the taxable year and that the expense was ordinary and necessary to [appellant's] business." Appellant has ultimately failed to show that the IRS made any adjustments to its original audit determination.

With respect to her contention that the third-party records appellant provides on appeal (various financial statements, receipts, and ledgers that document and categorize the expenses listed on appellant's return, and bank and credit card statements) support her claimed expenses and deductions, appellant has not provided the required substantiation for those expenses. Appellant attributed expense claims to various categories, including automative costs for ride-sharing services, online sales, a home office, meals, travel, charity, and medical expenses. For some of the ledger entries, there are also broadly encompassing descriptions, such as "supplies," "sales," or "training." However, appellant's evidence, in total, fails to adequately trace any of the enumerated expenses to specific business purposes or show whether the claimed expenses were ordinary or necessary. For certain categories, such as meals and home office expense, it is particularly unclear whether many of the ledger entries instead represent nondeductible personal expenses. (See IRC, § 262(a).) As to the expenses specifically related to travel and vehicle use, appellant provides no documentation to meet the heightened substantiation requirements under IRC section 274(d). Additionally, appellant provides no employer reimbursement policy to support the listed employee expenses, as requested by FTB on appeal.³ In summary, appellant has not shown error in FTB's determination to follow the federal disallowance of \$24,962 of claimed expenses and itemized deductions.

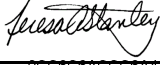
³ In FTB's opening brief, it invites appellant to provide the required documentation from her employer, such as the employer's reimbursement policy and the necessary verification from her employer regarding her claimed travel, vehicle, and other expenses to substantiate the claimed expenses and deductions. Appellant did not file a reply brief or submit any of the requested evidence.

HOLDING


Appellant has not shown error in FTB’s proposed assessment, which is based on final federal adjustments.


DISPOSITION

OTA sustains FTB’s action.

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Teresa A. Stanley
Administrative Law Judge

We concur:

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Erica Parker
Hearing Officer

DocuSigned by:

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Sheriene Anne Ridenour
Administrative Law Judge

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