

# What's New and Other Important Information for 2004?

## Amnesty

Recent legislation authorizes the Franchise Tax Board and the Board of Equalization to administer a Tax Amnesty Program. Tax amnesty is a limited-time chance for individuals and businesses to pay past-due income, franchise, sales, or use taxes and the related interest penalty-free without the fear of criminal prosecution. Amnesty runs from February 1, 2005, through March 31, 2005. Taxpayers eligible to participate in amnesty but choose not to do so will be subject to additional penalties.

Amnesty is open to both individuals and businesses for taxable years 2002 and prior, if they did any of the following:

- Did not file required California tax returns.
- Underreported income on a previously filed tax return.
- Claimed excessive deductions.
- Did not pay income/franchise, sales, or use taxes on time.

The following taxpayers or transactions are not eligible for amnesty:

- Taxpayers currently under criminal investigation or prosecution on tax-related matters.
- Abusive tax shelter transactions that were eligible for relief under California's Voluntary Compliance Initiative or the 2003 IRS Offshore Voluntary Compliance Initiative. These initiatives applied to taxpayers with nonreported or underreported tax liability amounts attributable to an investment in an abusive tax shelter. Note: These taxpayers are eligible for amnesty for non-abusive tax shelter items.

For more details, visit our Website at [www.ftb.ca.gov](http://www.ftb.ca.gov) or call (800) 852-5711.

## Tax Shelters

If you were involved in a potentially abusive tax shelter, you may have a disclosure, registration, and list maintenance requirement. The Franchise Tax Board may impose several new and enhanced penalties if you fail to file IRS Forms 8886, 8264, 8271 or any required information. For more information, see Registration and Reporting Requirements under Abusive Tax Shelters on our Website at [www.ftb.ca.gov](http://www.ftb.ca.gov).

## Differences between California and Federal Law

In general, California law conforms to the Internal Revenue Code (IRC) as of January 2001. However, there are continuing differences between California and federal law. When California conforms to federal tax law changes, we do not always adopt all of the changes made at the federal level. For more information regarding California and federal law, please visit our Website at [www.ftb.ca.gov](http://www.ftb.ca.gov) and select "Law and Legislation." Additional information can be found in FTB Pub. 1001, Supplemental Guidelines to California Adjustments, the instructions for California Schedule CA (540 or 540NR), and the Business Entity tax booklets.

Note, the instructions provided with California tax forms are a summary of California tax law and are only intended to aid taxpayers in preparing their state income tax returns. We include information that is most useful to the greatest number of taxpayers in the limited space available. It is not possible to

include all requirements of the California Revenue and Taxation Code (R&TC) in the tax booklets. Taxpayers should not consider the tax booklets as authoritative law.

## 2004 Tax Law Changes

**Federal Conformity Items – California has conformed to the Military Family Tax Relief Act (Public Law 108-121 to allow the following:**

- A deduction in computing adjusted gross income for certain trade or business expenses of members of the Armed Forces of the U.S.
- An exclusion from gross income for certain death benefits payable by reason of the death of astronauts.
- An exclusion for certain military fringe benefits.
- A 5-year period of suspension for excluding gain from the sale of a principal residence if the taxpayer's spouse is serving in the uniformed services or the Foreign Service of the U.S.
- An exclusion for certain military death gratuity payments from gross income.
- An exclusion for death gratuity income received by living survivors of military personnel who lost their lives on or after September 11, 2001.
- For tax years beginning in 2004 and 2005, the American Jobs Creation Act of 2004 allows taxpayers to elect to take state and local general sales and use taxes as an itemized deduction, instead of taking an itemized deduction for state and local income taxes. The Act gives taxpayers a choice of deducting actual taxes or tabular amount, increased by certain actual taxes. California has not conformed to this Act.

## New Form 540 2EZ income limitations

For taxable years beginning on or after January 1, 2004, you may be able to file Form 540 2EZ if you are single or head of household and your total income for the taxable year is \$100,000 or less, or if you are married filing jointly or qualifying widow(er) and your total income for the taxable year is \$200,000 or less. Total income is defined as wages, interest, dividends, and pension income. However, if income adjustments are required due to differences between California and federal law, you may not use this form. Get Form 540, e-file, or CalFile instead.

## Military Personnel

Servicemembers domiciled outside of California, and their spouses, may exclude the member's military compensation from gross income when computing the tax rate on nonmilitary income. Requirements for military servicemembers domiciled in California remain unchanged. Military servicemembers domiciled in California must include their military pay in total income. In addition, they must include their military pay in California source income when stationed in California. However, military pay is not California source income when a servicemember is permanently stationed outside of California. For more information, get FTB Pub. 1032, Tax Information for Military Personnel.

## Alimony Deduction

If you were a nonresident of California in 2004, you are now entitled to an alimony deduction. The deduction for alimony payments is allowed to a nonresident or part-year resident in the same ratio that "California AGI" for the entire year, computed without regard to the alimony deduction, is to "Total AGI" for the entire year, computed without regard to the alimony deduction.

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Changes in the Child and Dependent Care Expenses Credit:

- Earned income must have a source in California
- Dependent Care must be provided in California

### **Paid Family Leave Benefits**

If you received paid family leave benefits in 2004, they are not taxable by California. For additional information, get Schedule CA 540 and instructions – California Adjustments, and FTB Pub. 1001 – Supplemental Guidelines to California Adjustments.

### **Claim of Right**

If you had to repay an amount that you included in income in an earlier year, under a claim of right, you may be able to deduct the amount repaid from your income for the year in which you repaid it. Or, if the amount you repaid is more than \$3,000, you may be able to take a credit against your tax for the year in which you repaid it. For more information, go to Schedule CA, line 40 instructions.

### **Punitive Damages**

For court actions filed after August 16, 2004 and finally adjudicated by June 30, 2006, 75 percent of punitive damage awards must be paid to the Director of the California Department of Finance (DOF). You may exclude from income the portion of a punitive damage award that is paid to the DOF.

## **Other Important Information**

### **San Joaquin Levee Break**

If you were a victim of the San Joaquin levee break, get FTB Pub. 1034, California Disaster Relief Tax Provisions and Pub. 1034A-6, San Joaquin Levee Break, for more information.

### **Mandatory e-file**

California law requires individual income tax returns prepared by certain tax practitioners to be e-filed. This law saves money and resources for the state. If you have a tax practitioner prepare your return, they may be required to e-file it. You have the right to choose not to e-file, however, we encourage you take advantage of everything e-file has to offer.

### **Vehicle License Fee (VLF) Refund**

If you paid a VLF and deducted the fee as an itemized deduction for 2003, the VLF refund you received in 2004 is treated as a recovery of the amount you claimed as an itemized deduction. For more information, get Schedule CA 540 and instructions – California Adjustments, and FTB Pub. 1001, Supplemental Guidelines for California Adjustments.

### **Teacher Retention Credit**

The Teacher Retention Credit is suspended for tax years 2004 and 2005.

### **Net Operating Loss**

For taxable years beginning on or after January 1, 2004, California has reinstated the Net Operating Loss (NOL) carryover deduction. The carryover periods for NOL deductions that were incurred:

- Beginning before January 1, 2002, has been extended for two years.
- Beginning on or after January 1, 2002, and before January 1, 2003, has been extended for one year.

### **Natural Heritage Preservation Credit**

Currently, there is no funding to award Natural Heritage Preservation Credits. Therefore, no new credits may be claimed for 2004. However, carryover of previously awarded credits is not affected. Contact the Wildlife Conservation Board (WCB) to determine if funding has been restored, if they are accepting

qualified contributions of property, and to see if they are awarding new Natural Heritage Preservation Credits. Complete form FTB 3503 to claim the credit only if the WCB has resumed awarding the credits.

To get updated information regarding current funding, qualified contributions of property, or the awarding of credits, contact the Wildlife Conservation Board at (916) 445-8448. Or, go to their Website at [www.wcb.ca.gov](http://www.wcb.ca.gov).

### **New Voluntary Contribution Funds**

You may make voluntary contributions to the California Military Family Relief Fund and/or the California Prostate Cancer Research Fund.

### **TeleFile Discontinued**

TeleFile is no longer available to file California tax returns. We discontinued TeleFile due to decreasing usage and to help save California resources. If you qualified for TeleFile, you also qualify to use our free e-file options: CalFile. Like TeleFile, CalFile is fast, direct, and easy to use. Go to [www.ftb.ca.gov](http://www.ftb.ca.gov) to use CalFile or other free options available online including California e-file options and the Federal Free File Alliance.

### **Are you registered to vote?**

In order to vote in an election, you must be registered to vote at least 15 days before that election.

### **Common Errors and How to Prevent Them**

Help us process your return quickly and accurately. When we find an error, we must stop to verify the information on the return, which slows processing. The most common errors are claiming the wrong estimated tax payments, claiming the wrong exemption credit, claiming the wrong amount of real estate withholding, and making tax computation errors.

To avoid these errors and help us process your return faster, please use these helpful hints when preparing your return.

When claiming estimated payments:

- Verify that the amount of estimated payments claimed on your return matches what you sent to the FTB for that year. Check our Website at [www.ftb.ca.gov](http://www.ftb.ca.gov) and access the “Check Account Balance” feature to view your total estimate payments before you file your return.
- If the amount of estimated payments claimed on your tax return does not match FTB records, you will receive a Return Information Notice to explain the difference.

When totaling your exemptions:

- Be sure to add the exemption amounts correctly and transfer the total exemption amount to the correct line of the return. (See the individual line instructions for assistance).

When computing your tax:

- Check our Website at [www.ftb.ca.gov](http://www.ftb.ca.gov) and access the automated tax table to compute your tax, or
- Make sure to locate the correct tax amount from the tax table (in this booklet) and transfer it to your return correctly.

When claiming real estate withholding:

- Remember to claim the amount of withholding from real estate sold in California during 2004. Your escrow company should provide you with a California Form 593-B, Real Estate Withholding Tax Statement, indicating the amount withheld. For details, see the Form 540 line 40 instructions on page 20.

By using the helpful hints listed above, you can prevent delays in processing your return and unnecessary account adjustments.