

Tax News

October 2006

Contents

- Selvi Stanislaus confirmed as FTB executive officer
- New multi-agency *Offer in Compromise* form streamlines the process
- State announces 2006 income tax changes due to indexing
- Verify your client's estimated tax payments online
- *New e-services*
- Filing enforcement program's record-breaking year
- Bridging the tax gap
- Representing new business clients? Here are some helpful publications
- Criminal Corner
- The buzz on big business
Did your client qualify for the Manufacturers' Investment Credit?

Selvi Stanislaus confirmed as FTB executive officer

Selvi Stanislaus addressed the Senate Rules Committee on Wednesday, August 9, 2006, during the first part of her confirmation process. The committee voted unanimously to forward their recommendation for confirmation to the Senate, which also voted unanimously for confirmation.

On August 31, the California Senate confirmed Stanislaus as FTB's fourth executive officer, by a vote of 40-0.

In her August 9 speech to the Senate Rules Committee, Stanislaus summarized her accomplishments during her tenure as Executive Officer of the Franchise Tax Board. Here is the text of her August 9 speech to the Committee:

Thank you Chairman Perata, and members of the committee.

This past January, I was honored to be appointed by the three-member Franchise Tax Board as its fourth executive officer. I was humbled by the Board's unanimous confidence in me.

I want to thank Board of Equalization Chair John Chiang for his mentoring, support, and encouragement during my career at the BOE, and I want to thank Gerald H. Goldberg for his 25 years of steady leadership. He has provided me a strong foundation that I can build upon for the future.

My ultimate goal is to build a Franchise Tax Board that is even more responsive and effective to the needs of the Legislature, tax professionals, and, most importantly, responsive to the needs of California's taxpayers.

I believe one step forward in this process is through transparency in government, which I define as the ability of ordinary citizens to hold their government officials accountable for their actions. My husband and I immigrated to the United States because of the opportunities America offers. One reason we have such opportunities is that we have a more open government here. The fact that ordinary citizens have access to meetings, can request and receive government documents, and have input into government decisions is critical to my vision of a transparent FTB.

I have already directed staff to make more information available online. For example, we have posted legal rulings, senior management names and phone numbers, and more information about tax administration on the Web, which is a step in the right direction.

The FTB already has a well-deserved reputation for using technology to make our jobs easier, which makes the job of the taxpayers easier. But as we move forward with new technologies, we must do so with an ever-vigilant eye on protecting taxpayer's sensitive data.

Security is a great concern of mine. Lately it seems you can't pick up a newspaper or turn on a television without hearing about privacy, security, and lost or stolen data. I'm proud that the FTB follows a "defense in depth" security strategy, which is basically layers upon layers of security, with adherence to best practices from the government and private industry. We will continue to maintain our safeguards to protect the privacy of taxpayer records.

I will also continue to seek out program efficiencies and improve our customer service. Public trust is vital to the continued success of our voluntary self-assessed tax system, and I will strive to strengthen that trust. For example, "Tax News," our publication for tax professionals, is now available online, and updated as issues or changes emerge.

I am also committed to streamlining our processes and improving workflow to reduce the amount of time it takes to complete audits, protests, and appeals. This benefits the taxpayer, the tax professional, and the state.

I will continue to place a premium on customer service, and serving your constituents. When taxpayers contact us with their issues or concerns, it is imperative we get them the information they need or make the adjustments required to help them comply with their tax obligations in a fair, impartial, efficient, and complete fashion. Although I cannot promise that everyone will like the tax board, I do want to reduce the frustration people sometimes feel when dealing with us.

As I stated earlier, increasing the amount and quality of information on our Website plays a big role. Internally, we will continue to provide legislators and state departments with fast, accurate, and complete information. Because the sooner the Legislature has the needed data, the faster you can introduce your bill, or respond to a constituent concern.

In conclusion, let me just highlight a few of my accomplishments during my short time as executive officer. I have:

- Increased our outreach and education programs to the underserved communities. This includes providing tax information in other languages to better meet the needs of our non-English speaking taxpayers. I am proud to announce that we have recently translated the Homeowner and Renter Assistance Booklet into Chinese, Korean, and Spanish.
- Increased our Speakers' Bureau presentations to small businesses, and newly formed tax-exempt organizations to educate them on their tax filing responsibilities.

- Completed one of the most successful filing seasons in FTB history. In the month of April, personal income tax deposits were \$11.3 billion - a 40 percent increase over 2005. Personal income tax payments, excluding wage withholding, were \$27 billion for the period of January 1 through the end of June. And as of last week, we had issued more than 9 million refunds for an average of \$709 per refund.
- Begun the process of reviewing and rewriting some of the most common billing and information notices we mail to taxpayers, to ensure that taxpayers will find them easy to read and understand.
- Looked at innovative ways to help taxpayers self-audit through various pilot programs.
- And, I am currently reviewing our collection practices to make them more responsive.

I'd like to add a "thank you" to the tremendous staff of the Franchise Tax Board. I have been warmly embraced in my new role. The employees have consistently welcomed me with eagerness, kindness, and an enthusiasm for what we can accomplish together.

I am grateful to have the opportunity to work with such an extraordinary organization as the FTB, and I look forward to a future filled with challenges and successes.

Thank you.

New multi-agency *Offer in Compromise* form streamlines the process

The Board of Equalization (BOE), Employment Development Department (EDD), and Franchise Tax Board (FTB) have developed a single form, the *Multi-Agency Form for Offer in Compromise* (DE999CA), which can be submitted to any of the state's tax agencies.

Your clients may apply for an *Offer in Compromise* (OIC) under certain circumstances, when they are unable to pay their full tax liabilities to the state. The program allows taxpayers to negotiate a reduced amount of their non-disputed tax liabilities. The state will consider an OIC when it is unlikely that the tax liability can be collected in full, and the offered amount reasonably reflects collection potential.

The individual agencies must still negotiate each OIC separately for their respective taxes. For example, only FTB can negotiate a state income tax liability, and only the Board of Equalization can negotiate sales or use tax liability.

The form is available online at the California Tax Service Center (www.taxes.ca.gov), as well as at each of the three tax departments' Websites (BOE www.boe.ca.gov, EDD www.edd.ca.gov, and FTB www.ftb.ca.gov).

State announces 2006 income tax changes due to indexing

It may be four months away, but it's not too early to be thinking about your state income taxes. The good news is California's personal income tax brackets will be indexed by 4.8 percent for 2006, which means that some taxpayers will pay less in income taxes next year.

Indexing takes the inflation rate into account, and adjusts tax brackets, filing requirement thresholds, the standard deduction, and certain credits. FTB has computed the indexed values using the inflation rate of 4.8 percent, as measured by the California Consumer Price Index for all urban consumers from June 2005 to June 2006. Last year's inflation rate measured 2.8 percent.

State tax law indexes minimum filing requirement thresholds to ensure that most people who will not owe taxes are not required to file a tax return. We adjust the tables each year to include the added senior exemption, and the dependent exemption credits. The tax threshold is the amount of income reached where a tax liability is incurred. It has risen to \$11,271 of adjusted gross income for single and married filing separate taxpayers, and \$22,542 for married filing joint, surviving spouse, and head of household filers.

The standard deduction will increase for single or married filing separate taxpayers from \$3,254 to \$3,410. For married filing jointly, qualifying widow(er), or head of household taxpayers, the standard deduction increases from \$6,508 to \$6,820. The personal exemption credit increases for single, married filing separate, or head of household taxpayers from \$87 to \$91 and for married filing jointly or surviving spouses from \$174 to \$182. The dependent exemption credit changes from \$272 to \$285 for each dependent.

Other tax credits affected by indexing include the Joint Custody Head of Household Credit, Dependent Parent Credit, Qualified Senior Head of Household Credit, and the Renter's Tax Credit.

Refer to the chart below for tax rates and filing requirement amounts:

2006 California tax rate schedules

Schedule X					
Single, or married filing separate taxpayers					
If the taxable income is		Computed tax is			
Over	But not over				Of amount over
\$0	\$6,622	\$0.00	Plus	1.0%	\$0
\$6,622	\$15,698	\$66.22	Plus	2.0%	\$6,622
\$15,698	\$24,776	\$247.74	Plus	4.0%	\$15,698
\$24,776	\$34,394	\$610.86	Plus	6.0%	\$24,776

\$34,394 \$43,467	\$43,467 And over	\$1,187.94 \$1,913.78	Plus Plus	8.0% 9.3%	\$34,394 \$43,467
Schedule Y					
Married filing joint, or qualifying widow(er) taxpayers					
If the taxable income is		Computed tax is			
Over	But not over				Of amount over
\$0	\$13,244	\$0.00	Plus	1.0%	\$0
\$13,244	\$31,396	\$132.44	Plus	2.0%	\$13,244
\$31,396	\$49,552	\$495.48	Plus	4.0%	\$31,396
\$49,552	\$68,788	\$1,221.72	Plus	6.0%	\$49,552
\$68,788	\$86,934	\$2,375.88	Plus	8.0%	\$68,788
\$86,934	And over	\$3,827.56	Plus	9.3%	\$86,934
Schedule Z					
Head of household taxpayers					
If the taxable income is		Computed tax is			
Over	But not over				Of amount over
\$0	\$13,251	\$0.00	Plus	1.0%	\$0
\$13,251	\$31,397	\$132.51	Plus	2.0%	\$13,251
\$31,397	\$40,473	\$495.43	Plus	4.0%	\$31,397
\$40,473	\$50,090	\$858.47	Plus	6.0%	\$40,473
\$50,090	\$59,166	\$1,435.49	Plus	8.0%	\$50,090
\$59,166	And over	\$2,161.57	Plus	9.3%	\$59,166

2006 Filing requirement amounts

Gross income more than:

	Age on 12/31/06	No dependents	1 dependent	2 or more dependents
Single	Under 65	13,713	23,213	30,338
	65 or older	18,263	25,388	31,088
Head of household				

	Age on 12/31/06	No dependents	1 dependent	2 or more dependents
Married Married filing separate	Under 65 (both spouses)	27,426	36,926	44,051
	65 or older (one spouse)	31,976	39,101	44,801
	65 or older (both spouses)	36,526	43,651	49,351
Qualifying widow(er)	Age on 12/31/06			
	Under 65	N/A	23,213	30,338
	65 or older	N/A	25,388	31,088

Adjusted gross income more than:

	Age on 12/31/06	No dependents	1 dependent	2 or more dependents
Single Head of household	Under 65	10,970	20,470	27,595
	65 or older	15,520	22,645	28,345
Married Married filing separate	Age on 12/31/06			
	Under 65 (both spouses)	21,940	31,440	38,565
	65 or older (one spouse)	26,490	33,615	39,315
	65 or older (both spouses)	31,040	38,165	43,865
Qualifying widow(er)	Age on 12/31/06			
	Under 65	N/A	20,470	27,595
	65 or older	N/A	22,645	28,345

Verify your client's estimated tax payments online

Do you know that you can verify the total amount of estimated tax payments your client has made to Franchise Tax Board, before filing your client's return?

Using our online service, [View Payments and Balance Due](#), you can view the following transactions made by your client, provided we have not yet applied them to a tax year:

- The last 25 estimated tax payments.
- Estimated tax transfers.
- Extension payments.

By using this service before filing your clients' tax returns, you can virtually eliminate the possibility they will receive Return Information Notices because they claimed incorrect estimated tax payments on their tax returns. All you need is your client's permission, Social Security Number, and [Customer Service Number](#).

You can also use this service to:

- View the current balance due on your clients' accounts.
- View the 60 most recent payments applied to a balance due.
- Obtain tax year summary information on any tax year with a balance due.

Note: Because of our processing timeframes, it may take up to 45 days for payments to post to your client's accounts.

Go to www.ftb.ca.gov and click on the *Check Your Account* link in the *Tools* list.

New e-services

Subscription services

Earlier this year we introduced our new Subscription Services email service, which allows you to receive important tax information by email. Using this service you may subscribe, or unsubscribe to our *Tax News* or e-file News mailing lists. Once subscribed, you will automatically receive emails whenever we post information to either list.

- **Tax News**
Provides information on laws, legislation, programs, and services.
- **e-file News**
Provides information on e-file, e-Services, seminars, and processing developments.

Business e-file expands in 2007 filing season

Remember – for tax years beginning on or after January 1, 2006, businesses will also be able to e-file the return types below, in addition to the Form 100 *California Corporation Franchise or Income Tax Return*:

- Form 565 Partnerships.
- Form 568 Limited Liability Companies.
- Form 100S S-Corporation.

Check with your software providers to see if they support Business e-file.

Secure Web Internet File Transfer System (SWIFT)

SWIFT is a new secure file transfer system transmitters can use for transferring and retrieving confidential information via the Internet.

With SWIFT, transmitters can transfer personal and business e-file returns to us, and retrieve their e-file acknowledgment files. SWIFT supports large-file transfer, and is a quick, secure, and efficient method to meet the needs of the next generation of e-file. If you transmit returns to your software company, and they transmit them to FTB, you will probably not notice anything different because SWIFT does not affect how you interact with your software provider/transmitter. However, if your software currently allows you to transmit returns directly to Franchise Tax Board, you should contact your software provider/transmitter to ask if they plan to offer SWIFT as an option, and what may be required of you.

To subscribe, or get more information go to www.ftb.ca.gov and search for *Subscription Services*, *Business e-file*, or *SWIFT*.

Filing enforcement program's record-breaking year

The Franchise Tax Board's (FTB) filing enforcement (FE) program collected a record breaking \$524 million this past year. During fiscal year 2005-2006 our nonfiler program issued:

- 754,613 *Request or Demand for Tax Return* letters.
- 509,066 *Notices of Proposed Assessment*.

As of August 31, 2006, we have received approximately 200,000 tax returns.

Each year we receive more than 160 million information records. The records come from the Internal Revenue Service, the State Employment Development Department, the State Board of Equalization, employers, and banks. FTB also receives information on occupational licenses and mortgage interest payments. We match these records against our records of tax returns filed. If there is no return on file, we notify the taxpayer with a *Request or Demand for Tax Return* letter, and give them time to respond.

Taxpayers' top five reasons for explaining why they didn't file their tax returns on time:

1. "A major life event occurred." Divorce topped the list, with death of a loved one a close second.
2. "I didn't have the records needed to file."
3. "I didn't have the money to pay."
4. "Procrastination."
5. "I didn't have the tax forms."

Some of the more creative responses include "I have emotional problems concerning doing my taxes," and "This year I filed my return about a year sooner than last year." In other words, "I'm getting better!"

We continuously strive to improve our filing enforcement program, and the services that are available to both the taxpayer, and the tax preparer communities. Listening to the feedback we receive from preparers and taxpayers prompted us to implement some new services that you may not be aware of:

- **A 24x7 Website** at www.ftb.ca.gov/inc. At this Website, you can request additional time to file a tax return. This service may assist those who are experiencing a life crisis, or who need more time to obtain records to file a return.
- **An online application to request payment arrangements.** The application is available at www.ftb.ca.gov. Select the "Filing" tab at the top of the page. The link is located under "Paying your tax," "Request an installment agreement."
- **Online ability to respond to the *Request or Demand for Tax Return Letter*.** Either you or your client may access our 24x7 Website at www.ftb.ca.gov/inc. Enter the unique number from the letter, and select "I don't think I have a

requirement to file.” An online form will display, and guide you through providing the information we need to resolve your account. In most cases, if your client does not have a requirement to file, the case can be closed online, and you can print a confirmation letter from the Website.

We realize that our annual filing enforcement process can have a great impact on the tax preparer community. If you have any suggestions for improvements, we'd love to hear from you! Please contact Kurt Vickner at kurt.vickner@ftb.ca.gov with your suggestions and ideas.

Bridging the tax gap

In previous issues of *Tax News*, we identified components of the Tax Gap (July 2006), common types of underreported income (August 2006), and common mistakes made in reporting expenses (September 2006). So, what is the FTB doing to bridge the tax gap?

We have mobilized compliance groups to focus on key contributors to the tax gap. Each compliance group identifies the enforcement and taxpayer education efforts to deal with these areas of noncompliance:

- **Fraudulent Tax Preparers** - Focuses on detection, enforcement, and remediation of tax preparers who persistently underreport income, and overstate expense deductions.
- **Underreported Income** - Uses existing departmental data in different ways to identify taxpayers who underreport income. Recognizing what taxpayers fail to report requires new detection methods and audit techniques.
- **Abusive Tax Shelters** - Concentrates on combating abusive tax avoidance transactions.
- **Abusive Tax Shelter Promoters** - Sets up penalties on practitioners and advisors who promote potentially abusive tax shelters.

In addition to creating these targeted noncompliance groups, we are expanding our existing activities and programs by:

- Establishing more education and outreach programs to increase public awareness of the Tax Gap, and its effect on California and its taxpayers.
- Conducting more audits on sole proprietors. Most analyses of the tax gap estimate that sole proprietors make up the highest percentage of individual taxpayers who underreport their income. We are specifically looking at sole proprietors of businesses with a high potential of underreporting their income or overstating expense deductions. Businesses with sizeable cash transactions tend to have a higher percentage of under-reported income.
- Encouraging voluntary compliance. We send letters to notify individuals of potential noncompliance items on their return. This notification gives them the chance to amend their returns and correct errors, **before** we open an audit.
- Increasing income-matching efforts using federal Form 1099s, W-2s, and other information shared by government agencies to identify California nonfilers, and underreported income.

FTB plans to collaborate with the Internal Revenue Service on tax gap issues. Through these efforts, both individually and jointly, FTB will continue to identify and remove areas of noncompliance contributing to the Tax Gap.

Representing new business clients? Here are some helpful publications

If you have new business clients, you may be looking for some quick information on California business tax law. Here are some FTB publications that can give you a head start in finding answers to your questions.

Publication 1060 *Guide for Corporations Starting Business in California* (<http://www.ftb.ca.gov/forms/misc/1060.pdf>) is a guide designed to help you file your first:

- *California Corporation or Franchise Return*, Form 100.
- *California S Corporation or Franchise Return*, Form 100S.
- *Bank and Corporation Estimated Tax Payment Voucher*, Form 100-ES.

It's only seven pages, but you will find valuable information in this guide to help you understand the basis of the tax, how to request forms and instructions, file tax returns correctly, and avoid unnecessary penalties and interest.

If you want to determine if your client has a California filing requirement, start by looking at FTB's *Questionnaire Regarding Activities in California*. [Note: this questionnaire is obsolete as of 8/24/2009]. We send this questionnaire to corporations we believe have a California filing requirement, that haven't filed California returns, but answering its questions may help you determine your clients' California filing requirements.

If you are certain your business clients have a California filing requirement, but you need more information on tax law for corporations, refer to Publication 1063, *California Corporation Tax Law: A Guide for Corporations* (<http://www.ftb.ca.gov/forms/misc/1063.pdf>). In this compact guide, you will find definitions of key terms, discussions of laws governing franchise tax, income tax, combined reporting, apportionment of income, and more.

Consult Publication 1068, *Exempt Organizations - Requirements for Filing Returns and Paying Filing Fees* (<http://www.ftb.ca.gov/forms/misc/1068.pdf>) for information on exempt corporations.

You can find valuable information on dissolution or tax clearance requirements in our Publication 1038 series (1038, 1038A, L, and T). From the FTB 2006 Forms page, (http://www.ftb.ca.gov/forms/06_forms/index.html) scroll down to the 1038 series. For suspended corporations, call Business Entity Collections at **888-635-0494**.

Finally, don't forget to bookmark the *Tax News Web Page* (<http://www.ftb.ca.gov/professionals/taxnews/index.html>) for a quick shortcut to a wide range of useful California tax information. You will also want to bookmark the newly remodeled *California Tax Service Center* (CTSC) Website, (<http://www.taxes.ca.gov/index.html>) formerly the *California Tax Information Center*. This Website offers one-stop shopping for information about income tax, payroll taxes, and

sales, use, property, and special taxes. The Board of Equalization, Employment Development Department, and Franchise Tax Board contribute to this Website, and each department provides contact information. The CTSC Website also links to IRS Forms.

For urgent questions, and issues not covered by our publications, call our Tax Practitioner Hotline at (916) 845-7057.

Criminal Corner

We are committed to closing California's \$6.5 billion tax gap, defined as the difference between tax that is owed and tax that is paid. Our special agents work cooperatively with law enforcement agencies throughout California to uncover illegal behaviors that contribute to the tax gap. These include underreporting income, overstating deductions, failing to file returns, failing to pay taxes due, and making illegal cash payments to employees.

Tax fraud is not a victimless crime. You can report suspected tax fraud by calling FTB at (800) 540-3453.

Cases prosecuted in the last month are described below.

San Jose couple sentenced for felony tax evasion

On August 4, 2006, the State Board of Equalization (BOE) announced the sentencing of Larry and Patricia Stenshoel after the couple was convicted of two felony counts of sales tax evasion, three felony counts of state income tax evasion, and one count of grand theft.

Larry Stenshoel was sentenced to two years in state prison. Patricia Stenshoel was sentenced to three years probation and 1,440 hours of community service. Additionally, Larry and Patricia Stenshoel were ordered to pay remaining restitution of \$544,834 to the BOE and \$264,246 to the Franchise Tax Board (FTB). They had initially paid \$500,000 toward their tax debt. The case was prosecuted by the Santa Clara County District Attorney's Office.

Larry Stenshoel, 76, and his wife, Patricia Stenshoel, 72, operated the Cade Company, a San Jose waterproofing business, where they charged and collected sales tax from customers without properly paying the tax to the BOE. The joint investigation conducted by the BOE and the FTB found the Stenshoels intentionally failed to report and pay more than \$430,000 in sales tax from October 1996 to December 1997 and more than \$60,000 in State income taxes between 1994 and 1996.

The Stenshoels fled California after charges were filed against them in April 2001. Larry Stenshoel was extradited from the state of Texas in June 2005, and Patricia Stenshoel later surrendered to authorities in February 2006.

Orange county man convicted for unpaid income taxes

An Orange County man awaits sentencing after he was found guilty on five counts of felony state income tax evasion.

David D. Detar, 50, an independent salesman who worked for numerous businesses in Orange County, was convicted of tax evasion for failure to file state income tax returns for 1998 through 2002. At his trial, six of his former employers testified they issued

Form 1099s to Detar. After the prosecutor submitted 35 pieces of evidence Orange County Superior Court Judge Byron McMillan addressed Detar and said, "I can't find one reason to not find you guilty."

Detar failed to report more than \$207,000 in income for 1998 through 2002 state income tax returns, and owes the FTB more than \$16,000 in unpaid tax, penalties, interest, plus the cost of the investigation.

Detar faces a maximum sentence of 15 years in state prison. This was a joint case with the Orange County District Attorney's Office, and the FTB.

Illegal cigarette sales burn San Gabriel woman

A San Gabriel woman, involved in selling illegal cigarettes, was sentenced to three years in state prison on filing false state income tax returns.

Nancy N. La, 56, failed to report more than \$2 million in income on her jointly filed 2001 and 2002 state income tax returns, and owes the FTB more than \$427,000 in unpaid tax, penalties, interest, and the cost of the investigation. Forensic auditors examined the defendant's bank records and business financial records to determine how much tax was owed.

The total amount of restitution will be determined at La's restitution hearing on November 13, 2006.

The buzz on big business

Did your client qualify for the Manufacturers' Investment Credit?

A brief history

The Manufacturer's Investment Credit (MIC) became effective on January 1, 1994, and was repealed effective January 1, 2004. Although repealed, Revenue and Taxation Code Section 23649(h) allows the MIC to be carried forward for seven or nine years, for qualifying small businesses. Thus, the MIC can be carried forward through the **end** of taxable years beginning on or after January 1, 2010, or January 1, 2012. Recent State Board of Equalization (BOE) decisions have clarified qualifying taxpayers' ability to claim the MIC.

Definitions

Qualified taxpayer

A *qualified taxpayer* must be engaged in at least one line of business described in Standard Industry Code (SIC) 2000 through 3999, or 7371 through 7373 for taxable years beginning on or after January 1, 1998. The SIC codes are listed in the *SIC/NA/ICS Manual*, 1987 edition (http://www.osha.gov/pls/imis/sic_manual.html).

Qualified costs

To qualify for the credit, *qualified costs* must meet *all* of the following criteria:

- The cost was incurred for acquiring, constructing, or reconstructing qualified property. The cost must have been paid or incurred on or after January 1, 1994.
- The taxpayer paid California sales or use tax on qualified property, either directly or indirectly, *except* for capitalized labor.
- Amounts paid or incurred for qualified property must be chargeable to the taxpayer's capital account (usually depreciable), *except* for certain operating leases.
- Qualified costs may also include capitalized labor costs that are *directly* allocable to constructing or modifying qualified property.

Qualified property

Generally, *qualified property* is tangible personal property as defined in Internal Revenue code Section 1245(a), which is used more than 50 percent of the time in a manufacturing, or other related qualified activity.

Qualified activities include:

- Manufacturing, processing, refining, fabricating, or recycling.
- Research and development.
- Maintaining, repairing, testing, or measuring other qualified property.

- Pollution control (meeting or exceeding established state or local standards.)

See our brochure (FTB 113), <http://www.ftb.ca.gov/forms/misc/1113.pdf>, for answers to frequently asked questions about the MIC.

How does all this affect my clients?

Generally, a qualified taxpayer was allowed a MIC equal to six percent of the qualified costs paid or incurred for California qualified property (see definitions above).

The MIC could be claimed for:

Taxable years beginning on or after:	Qualified costs incurred:		Qualified property placed in service:	
	After	Before	After	Before
January 1, 1995	January 1, 1994	January 1, 2004	January 1, 1994	January 1, 2004

In the *Appeal of Save Mart Supermarkets & Subsidiary* 2002-SBE-002, February 6, 2002, BOE addressed a *qualified taxpayer* issue. Its decision asserted that the activities of a full-service bakery and meat-processing department operating within a grocery store met the criteria for a qualified taxpayer. BOE determined the taxpayer engaged in activities described in Division D of the *SIC/NAICS Manual* (http://www.osha.gov/pls/imis/sic_manual.html). In addition, BOE found that the bakery and meat operations were more than a “trifling or irrelevant” segment of its overall operations.

BOE again addressed the status of qualified taxpayer in an unpublished 2005 decision, stating that the taxpayer was a qualified taxpayer, and observing that:

... although our *Save Mart* opinion serves as a precedent in other matters involving the same facts; i.e., other grocery stores with meat and bakery departments, its application under other facts; i.e., with respect to delicatessens and restaurants, among other things, has not been decided by this Board. As a result, if the qualified taxpayer issue is raised in other factual contexts, our analysis in *Save Mart* will certainly serve to guide us, but will not necessarily require a specific outcome, as we will need to examine the activities as alleged in light of the R&TC Section 23649 and *Save Mart*.

Your client may have qualified for the MIC, if:

- Based on the language of these BOE decisions, your client had activities described in Division D of the SIC/NAICS Manual.
- The activity was a significant part of your client’s overall operations.
- Your client paid or incurred qualified costs during the period that the MIC statute was in effect, for California qualified property placed into service after January 1, 1994, and before January 1, 2004.

FTB will give full weight and consideration to these BOE decisions. If you have clients who claimed the MIC on their original return,

- Or on an amended return.
- Or who wish to claim the MIC by filing a claim for refund (assuming the statute of limitations has not expired).

They must show they were qualified taxpayers, and that they paid, or incurred qualified costs for qualified property placed into service in California before January 1, 2004.

If your client is under examination, FTB will consider using sampling techniques, or other methods to examine the MIC assets. This will allow us to obtain the information we need to support the qualified costs and qualified property claimed by your client, while minimizing intrusiveness on your client.