Tax News

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Contents

Page

New Home Tax Credits Available 2

Withholding Agents Who Fail to Withhold 4

Available Now: Free California Source Income Withholding Webinars 6

Consider an Installment Agreement for Your Clients with Tax Bills 6

IRS Nationwide Tax Forums Registration Available! 8

Small Business Fair 8

2009 Bill of Rights Annual Report 8

Small Business
If Your Clients Have an Online Business - They May Owe State Taxes 9

Ask the Advocate
Doing Business 10

Inside FTB
Conformity Newsflash 11

Criminal Corner
Malibu Man Gets Five Years Probation for Grand Theft and Tax Charges 13

New Home Tax Credits Available

The 2010 New Home/First Time Buyer tax credits are available for taxpayers who purchase a qualified principal residence on or after May 1, 2010, and before January 1, 2011. Additionally, these tax credits are available for taxpayers who purchase a qualified principal residence on or after December 31, 2010, and before August 1, 2011, pursuant to an enforceable purchase agreement executed on or before December 31, 2010. The purchase date is defined as the date escrow closes.

These tax credits are limited to the smaller amount of five percent of the purchase price or $10,000 for a qualified principal residence. Taxpayers must apply the total tax credit in equal amounts over three successive tax years (maximum of $3,333 per year) beginning with the tax year in which the home is purchased. The tax credits cannot reduce regular tax below tentative minimum tax (TMT). The tax credits are nonrefundable and the unused credits cannot be carried over.

The total amount of allocated tax credit for all taxpayers may not exceed $100 million for the New Home Credit and $100 million for the First-Time Buyer Credit. However, since many taxpayers will not be able to utilize the entire tax credit, the legislation specifies that the $100 million cap for the New Home Credit will be reduced by 70 percent of the tax credit allocated to each buyer and the $100 million cap for the First-Time Buyer Credit will be reduced by 57 percent of the tax credit allocated to each buyer. We will allocate the tax credits on a first-come, first-served basis.

Only one tax credit is allowed per taxpayer. If a taxpayer qualifies for both tax credits, the law specifies that we will allocate the amount under the New Home Credit.

Taxpayers will **not** be eligible for either tax credit if any of the following apply:

- The taxpayer was allowed a 2009 New Home Credit.
- The taxpayer is under 18 years old. (A taxpayer who is married as of the date of purchase will be considered to be 18 if the spouse/registered domestic partner (RDP) of the taxpayer is 18 or older on the date of purchase.)
- The taxpayer or the taxpayer's spouse/RDP is related to the seller.
- The taxpayer qualifies as a dependent of any other taxpayer for the tax year of the purchase.

New Home Credit: A qualified principal residence, for purposes of the New Home Credit, must:

- Be a single family residence, either detached or attached.

- Have never been occupied. Sellers must certify that the home has never been occupied in order for a taxpayer to receive an allocation of the credit.
- Be eligible for the California property tax homeowner's exemption.
- Be occupied by the taxpayer as their principal residence for a minimum of 2 years immediately following the purchase.

Tax credit allocation:

- A Certificate of Allocation will not be issued if:
    - The seller does not certify the home has never been occupied.
    - We do not receive the application and a copy of the properly executed settlement statement within two weeks (14 calendar days) after the close of escrow.
    - We receive the application or reservation request after the total tax credits available have been allocated.
- Our determination may not be protested or appealed.

First-Time Buyer Credit: A qualified principal residence, for purposes of the First-Time Buyer Credit, must be:

- A single family residence, either detached or attached.
- Eligible for the California property tax homeowner's exemption.
- Occupied by the taxpayer as their principal residence for a minimum of 2 years immediately following the purchase.

A first-time buyer is any individual (and the individual's spouse/RDP, if married) who did not have an ownership interest in a principal residence during the preceding three-year period ending on the date of the purchase of the qualified principal residence. If the buyer is married on the date of purchase and either the buyer or the buyer's spouse/RDP had an ownership interest in a principal residence during the preceding three-year period, the buyer does not qualify for the First-Time Buyer Credit even if the spouse/RDP is not going to be on title.

Tax credit allocation:

- A Certificate of Allocation will not be issued if:
    - We do not receive the application and a copy of the properly executed settlement statement within two weeks (14 calendar days) after the close of escrow.
    - We receive the application after the total tax credits available have been allocated.
- Our determination may not be protested or appealed.

Applications: We started accepting applications, FTB 3549-A, Application for New Home / First-Time Buyer Credit, on May 1, 2010. Do **not** use the 2009 application. Check our website for the most recent updates.

Reservations: Taxpayers who qualify for the **New Home Credit** may, but are not required to, reserve a tax credit prior to the close of escrow. Reservations will become important as we near the $100 million cap for homes that may not close escrow before the cap is reached. To reserve a tax credit, the taxpayer and seller need to complete, sign, and submit to us a reservation request to certify that they have entered into an enforceable purchase agreement on or after May 1, 2010, and on or before December 31, 2010. A copy of the signed contract must be included with the reservation request, FTB 3549-RR, Reservation Request for New Home Credit.

If you are only applying for the **First-Time Buyer Credit,** you will **not** be able to reserve the tax credit before escrow closes.

Claiming the tax credit:

- The taxpayer must receive a Certificate of Allocation from us to claim the tax credit on their California personal income tax return. The Certificate of Allocation will state the maximum amount the taxpayer can claim listed by tax year.
- The taxpayer should refer to the 2010 New Home / First-Time Buyer Credit Publication for instructions on claiming the tax credit (the publication will be available by December 2010).
- Special rules apply to married/RDP taxpayers filing separately, in which case each spouse/RDP is entitled to one-half of the tax credit, even if their ownership percentages are not equal. For two or more taxpayers who are not married/RDP, the tax credit amount will have already been allocated to each taxpayer occupying the residence on their respective tax credit allocation letter.
- If the available tax credit exceeds the current year net tax, the unused tax credit may **not** be carried over to the following tax year.
- The tax credit may not reduce regular tax below TMT.
- The tax credit is **not** refundable.
- Any disallowance of the tax credit may not be protested or appealed.

Applying for the 2010 New Home/First Time Buyer tax credits: Applications must be submitted **after** escrow closes. Fax the completed Form 3549-A and the final settlement statement (generally the buyer's HUD-1 statement) to us at **916.855.5577**.We will deny the application if the 2009 form is used. For more information, go to ftb.ca.gov and search for home tax credits.

Withholding Agents Who Fail to Withhold

A withholding agent is required to withhold seven percent from all payments or distributions of California source income made to a nonresident payee unless the withholding agent receives authorization from us for a waiver or reduced withholding amount.[1]

A withholding agent who fails to withhold, under withholds, or fails to remit withholding is liable for the greater of:

- The amount actually withheld.
- The amount of taxes due from the nonresident, but not more than the amount required to be withheld.[2]

Enforcement of withholding responsibilities

We actively pursue and assess liabilities on withholding agents that failed to comply with their withholding responsibilities. R&TC Section 18662(d) allows us to assess a liability for withholding when required, plus interest at the adjusted annual rate unless it is shown that the failure is due to reasonable cause. The liability is the maximum amount required to be withheld. R&TC Section 19183 allows us to assess a penalty for each information return not filed. The penalty is $100 for each payee.

Need more information about withholding?

Web: Go to ftb.ca.gov and search for **nonresident withholding**.
Phone: 888.792.4900 (Within the U.S.)
916.845.4900 (Outside the U.S.)
Fax: 916.845.9512
Email: wscs.gen@ftb.ca.gov
(This is not a secure email address. Please do not send confidential information.)

[1] California Revenue and Taxation Code (R&TC) Section 18662
[2] R&TC Section 18668

Available Now: Free California Source Income Withholding Webinars

We will host free California source income withholding webinars in May 2010. The topic is:

Independent Contractor Withholding
We designed this webinar for those who must withhold on California source income payments to resident and nonresident independent contractors. We'll take a look at:

- The basics of resident and nonresident independent contractor withholding, including backup withholding.
- A summary of the three phases of withholding and what to do before payment (FTB Forms 587, 588, 589, 590), at the time of payment, and after payment of California source income to independent contractors (FTB Forms 592, 592-V, 592-B).
- How we're preparing for process changes that will occur when we implement our new, automated withholding system in late 2010.
- Withholding resources and contact information you can use at any time.

Dates/Times: Wednesday, May 5, 2010, 10 a.m. (PST)
Wednesday, May 12, 2010, 1 p.m. (PST)

Duration: Approximately 40 minutes

Register here

Registration only takes a few minutes. Space is limited. To reserve your space, select the link above or go to ftb.ca.gov and search for **webinars**.

Consider an Installment Agreement for Your Clients with Tax Bills

Now that you've got those returns filed for your clients, some of them may be returning to your office with Statements of Tax Due from us. Some may have forgotten to send in a check, or if they were short on cash, they may have sent in a partial payment, or no payment at all resulting in the tax bill. The best advice you can give them is to contact us immediately to let us know the situation and to discuss payment options.

We offer a variety of methods your clients may use to pay the tax with a balance-due return. Individuals can use Web Pay, EFT, credit cards, Western Union, and checks or money orders. However, if your client is in a true financial crisis, he or she may be eligible to make monthly payments to us using an installment agreement.

To start the installment agreement process, an individual must first fill out a simple form to request an installment agreement. FTB Form 3567, Installment Agreement Request, can be completed online or mailed to us. An installment agreement can also be applied for by calling us at **800.689.4776**.

We normally grant an agreement without requiring financial information if an individual taxpayer:

- Owes a balance of $25,000 or less.
- Agrees to pay the full amount in 60 months or less.
- Has filed all required personal income tax returns.

Once the client has applied for an installment agreement, we will either approve or deny the agreement. In some cases, we will request additional financial information from your client. Our decision to approve the agreement is based on ability to pay and compliance history. When applying for the installment agreement, they client should provide complete information, including bank information for an automatic debit. Failure to provide complete information will delay and possibly cause us to deny the application.

If the application is completed online, the status can be checked by using the client's social security number and confirmation number found on installment agreement confirmation page. If the application was mailed or requested by phone, we send a written notification within 30 days. If you do not hear from us after 30 days, call us at **800.689.4776** during business hours. During this time, you should advise your client to begin making payments as proposed in the agreement application. If the installment agreement is approved, this amount will be due on a specific day each month for the duration of an agreement. Missing a payment or having a payment dishonored may result in the installment agreement being revoked or cancelled.

If your client is a business entity, they may also qualify for an installment agreement. Business entities must call us at **888.635.0494** to request an agreement.

IRS Nationwide Tax Forums Registration Available!

Join tax professionals from across the country for three days of the latest tax law information, hands-on workshops, networking opportunities, and exhibits of the latest tax products and financial services to improve your business.

In 2010, the Nationwide Tax Forums sites include Atlanta, GA, Chicago, IL, Orlando, FL, New York, NY, Las Vegas, NV, and finally San Diego, CA.

Take advantage of this great opportunity to receive CPE credits, learn from subject matter experts and, network with your peers. You can also take advantage of IRS electronic services and, obtain assistance on your most difficult tax case. More forum dates and information is available on our website. To register, go to the IRS Nationwide Tax Forum at irstaxforum.com.

Small Business Fair

The Riverside Small Business Fair is a special event designed to help small businesses by connecting them with representatives from over 40 federal, state, and local government agencies. It is essentially a one-stop opportunity to attend free workshops and efficiently gather free, valuable information that is tailored to the needs of small business.

The fair is Tuesday, May 25, 2010, from 4:30 p.m. to 7:30 p.m. at the Riverside Convention Center, 3443 Orange Street in Riverside, CA.

2009 Bill of Rights Annual Report

Read about what the Taxpayer's Rights Advocate is telling the Legislature on your behalf in the 2009 Bill of Rights Annual Report.

Small Business

If Your Clients Have an Online Business - They May Owe State Taxes

We, along with the California State Board of Equalization (BOE), urge online buyers and sellers to be informed about their tax obligations. The Internet is a dynamic and convenient technology that many businesses use to sell their products and that shoppers use to find great deals. However, one essential fact is often overlooked — there is no general tax exemption for sales made over the Internet.

We are jointly contacting Internet auction houses to provide them with educational material to help their customers meet their state tax responsibilities. We created a new publication designed to assist online buyers and sellers to understand their tax responsibilities, FTB 3730, Online Buying or Selling — Know Your Tax Obligation.

Sales Tax
The tax imposed on retail sales in California is called sales tax, and the retailer is responsible for reporting and paying the tax to the BOE. California retailers typically collect tax reimbursement from their purchasers for the sales tax these retailers owe. If a business is located in California, Internet sales of its physical products are generally taxable. For sales tax purposes, Internet sales are treated just like sales made at retail stores and other outlets. A seller's permit is generally required if a business makes three or more sales in a 12-month period. This applies even if sales are made through Internet auction houses or websites that offer online classified advertisements.

Use Tax
When a California purchaser buys from an out-of-state retailer who does not collect California tax on the sale, it is the responsibility of the individual purchasing the product to report use tax on the item paid. Use tax is simply a tax on the use, storage, or consumption of personal property in California. As an individual, use tax can be reported and paid either through a separate line designated for use tax on the California state income tax return or by filing a consumer use tax return directly with the BOE. If the purchaser is a retailer with a seller's permit, the use tax should be reported on the regular sales and use tax return.

Income Tax
In general, California taxes the income of residents on all of their income, regardless of source. A state tax return is due when an individual's income reaches certain levels. For 2009, a single person must file when his or her income reaches about $15,000. If you are an online auction seller and have exceeded this income level, you may have income tax obligations.

Additional Resources

FTB 988, California Use Tax & Your Filing Requirements

Publication 109, Are Your Internet Sales Taxable?
Publication 177, Internet Auction Sales and Purchases
Publication 110, California Use Tax Basics

For more information on other taxes and fees in California, go to taxes.ca.gov.

Ask the Advocate

Doing Business

As you know, I get many questions from practitioners about how to handle their client specific issues. This month, I received an interesting question from a practitioner in the bay area relating to "doing business." Does an out-of-state single member LLC that is disregarded for income tax purposes and whose only asset is a personal vacation home located out-of-state need to file a California LLC return and pay the annual tax if the single member/owner of the LLC is a California resident?

R&TC Section 17941 requires LLCs "doing business" in the State, as defined by Section 23101, to pay the annual tax. If the member of an LLC is "doing business" in California, the LLCs is "doing business" in California and subject to the annual tax. Likewise, if the LLC registers with the California Secretary of State, it must file and pay the $800 annual tax. So what is "doing business"? R&TC Section 23101 defines "doing business" as actively engaging in any transaction for the purpose of financial or pecuniary gain or profit. This is a facts and circumstances test.

The California residence of the sole member of a single member LLC, without more, does not mean that the LLC is "doing business" in California. But if that sole member, in his capacity as member of that LLC, has actively engaged in any transaction in California for the purpose of financial or pecuniary gain or profit, the LLC is "doing business" in California. Obviously, if the property was ever rented or even advertised for rent, then the basis for "doing business" may be there – depending on whether the single member actively engaged in a rent-related activity in California. But let's assume that the only use of the residence is personal use by the owner of the LLC. Expenses associated with mere ownership of property, such as paying taxes, do not usually rise to the level of "doing business."
So, which activities are enough to be considered "doing business"? This is where, sometimes, I must advise practitioners to weigh all of their client's facts and circumstances and take a filing position. As stated in FTB Notice 2009-8, the answers to

questions that depend principally on factual issues such as unity, residency, and doing business are no-ruling areas. We generally follow federal policy with respect to no-ruling areas and will ordinarily not issue Chief Counsel Rulings in certain areas because of the highly factual nature of the problems involved. In this case, it is up to the practitioner to interpret the law as it applies to the client's circumstances.

Steve Sims, EA
Taxpayers' Rights Advocate

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Inside FTB

Conformity Newsflash

On Tuesday, April 13, 2010, we sent our Tax News subscribers a newsflash on the recently signed SB 401, the Conformity Act of 2010. The Act changes California's conformity date to the Internal Revenue Code from January 1, 2005, to January 1, 2009, for taxable years beginning on or after January 1, 2010, except for the retroactive provisions explained below. California's conformity results in numerous substantive changes to the Personal Income Tax Law, the Administration of Franchise and Income Tax Law, and the Corporation Tax Law with respect to those areas of preexisting conformity that are subject to changes under federal laws enacted after January 1, 2005.

The following provisions of the new law affect taxable years beginning prior to January 1, 2010. We will provide additional updates about changes to the law for taxable years beginning on or after January 1, 2010.

Mortgage Forgiveness Debt Relief Extended
California law conforms, with modifications, to federal mortgage forgiveness debt relief for discharges occurring in tax 2007 through 2012. For more details regarding the mortgage forgiveness debt relief extension and how to file, go to our updated Mortgage Forgiveness Debt Relief webpage.

Income Exclusion of Federal Energy Grants
The Act provides that federal energy grants provided in lieu of federal energy credits are excluded from California gross income and alternative minimum taxable income of individuals and businesses. The income exclusion is applicable for any taxable year and is thus retroactive in its application.

Hokie Spirit Memorial Fund Exclusion
The Act allows a California taxpayer to exclude from gross income any amount received

from the Virginia Polytechnic Institute and State University, out of amounts transferred from the Hokie Spirit Memorial Fund established by the Virginia Tech Foundation. The income is excluded from gross income for any taxable year and is thus retroactive in its application.

Criminal Corner

Malibu Man Gets Five Years Probation for Grand Theft and Tax Charges

A Malibu man was given five years probation after pleading guilty to grand theft and filing false state income tax returns.

Dale Duko, 50, was also ordered to pay restitution of $36,168 to us for unpaid taxes, penalties, interest, and the cost of the investigation. According to court documents, Duko was employed as a manager of a local sound studio. Duko abused his position of trust by embezzling more than $230,000 from his employer during the years 1999 through 2006. Duko diverted payments made to his employer into his personal bank account. He failed to claim any of the embezzled income on his state income tax returns for the same period. All income is taxable, including income from illegal sources.

Los Angeles County Superior Court Judge David M. Horwitz handed down the sentence in Department 50 of the Clara Shortridge Foltz Criminal Justice Center. Los Angeles County Deputy District Attorney Serena Murillo prosecuted the case. This was a joint investigation between the Los Angeles County District Attorney's Office and us.