



# Tax News

## May 2012

Follow Tax News on Twitter at [twitter.com/CA\\_FTBTaxNews\\_E](https://twitter.com/CA_FTBTaxNews_E)

| <b>Contents</b>   | <b>Page</b> |
|---|-------------|
| New Top 500 Tax Debtors Unveiled  | 2           |
| Interactive Voice Response (IVR) Installment Agreement  | 3           |
| IRS Nationwide Tax Forums   | 3           |
| CSTC Summer Symposium 2012  | 4           |
| Strategic Plan Available Online   | 4           |
| <b>Tax News Flashes</b>   |             |
| IRS Penalty Relief to Farmers Affected by MF Global   | 5           |
| CSEA Super Seminars 2012  | 6           |
| Franchise Tax Board Updates Guidance on Real Estate Tax Deductions                                      | 6           |
| <b>Ask the Advocate</b>   |             |
| When Does an Out-of-State California Business or Individual Need to File a California Income Tax Return | 7           |
| <b>Event Calendar</b>   | 9           |
| <b>EDR in the News</b>  |             |
| FIRM  | 10          |
| <b>Criminal Corner</b>  |             |
| Orinda Physician Arrested on State Income Tax Charges   | 10          |
| <b>Big Business</b>   |             |
| Legal Issues New Guidance   | 11          |

## **New Top 500 Tax Debtors Unveiled**

We released our first Top 500 Delinquent Taxpayer list. A new law (Assembly Bill 1424 – Perea, Ch 455) expanded the list of the largest unpaid state income tax delinquencies from 250 to 500 and gave us additional enforcement tools.

The new law requires us to post a biannual list of the 500 largest state income tax debtors who owe more than \$100,000. In addition to updating the list twice a year, new provisions in the law include:

- Publishing the names and titles of corporate officers of listed corporations.
- Publishing professional license information.
- Returning noncompliant taxpayers to the list.
- Authorizing us to enter into reciprocal agreements with other states to offset refunds and collect tax debt.

Additional provisions effective July 2012:

- Working with state licensing agencies to suspend licenses held by the Top 500 including driver's licenses and occupational or professional licenses.
- Prohibiting state agencies from entering into contracts with the Top 500.

In November 2011, we mailed letters to individuals and businesses who could qualify to be listed if they do not resolve their outstanding liabilities. So far this year, we collected more than \$25 million in payments from individuals and businesses seeking to pay their tax debt and to prevent their names from being publicly posted on this list. More than \$118 million has been collected from the list since it was first posted in October 2007.

Taxpayers on the Top 500 list will be removed once the tax is paid or the taxpayer agrees to make payments under an approved installment agreement or offer in compromise. Tax liabilities under appeal, in litigation, or in bankruptcy proceedings are not included on the list.

Individual taxpayers on the list can contact us at 888.426.8555 to resolve their accounts. Business taxpayers can call 888.426.8751.

The [complete list](#) will be refreshed in October on our website at [ftb.ca.gov](http://ftb.ca.gov). The Board of Equalization (BOE) has a [similar list](#) of the state's top sales and use tax delinquencies, which is updated quarterly.

## **Interactive Voice Response (IVR) Installment Agreement**

As of March 12, 2012, taxpayers are able to request an installment agreement through our IVR system.

IVR Installment Agreement (I/A) provides an enhanced application to support installment agreement requests for taxpayers.

Taxpayers who call will have their eligibility verified during the IVR I/A process and ineligible taxpayers will be routed to an agent. This service will be available during normal business hours, evenings, and weekends. After hours, ineligible taxpayers will be advised to call back during normal business hours.

For information regarding IVR I/A, go to [ftb.ca.gov](http://ftb.ca.gov) and search for **installment agreement request**.

- Taxpayers call us at: 800.689.4776, weekdays, 8 a.m. to 5 p.m., except state holidays.
- Fax: 916.845.0993
- Mail: Franchise Tax Board, PO Box 2952, Sacramento CA 95812-2952

---

## **IRS Nationwide Tax Forums**

**Tax Forums registration is now open!** 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 newest products and services to improve your business.

In 2012, the IRS Nationwide Tax Forums will visit the following cities:

Orlando, FL – June 19 - 21  
Atlanta, GA – July 10 - 12  
San Diego, CA – July 17 - 19  
Las Vegas, NV – July 31 - August 2  
Chicago, IL – August 21 - 23  
New York, NY – August 28 - 30

Take advantage of this great opportunity to receive up to 18 CPE credits, network with your peers, learn from subject matter experts from the IRS as well as from our national association partners, or receive assistance on your most difficult case on site.

|                                 |       |
|---------------------------------|-------|
| Pre-registration                | \$211 |
| Members of partner associations | \$201 |
| On-site or late registration    | \$340 |

For more information or to register, visit the [Nationwide Tax Forum website](#).

---

## **CSTC Summer Symposium 2012**

[Register](#) for the California Society of Tax Consultants' Summer Symposium offered in Reno, NV on June 3 - 6, 2012.

---

## **Strategic Plan Available Online**

We are pleased to announce our new [Strategic Plan](#) is posted to our website. The plan covers the period of 2012 through 2016 and directs our long term goals and strategies to achieve the highest levels of service and excellence in tax administration for state government and California's taxpayers. The cornerstone of our mission statement – helping taxpayers file accurate and timely returns and pay the proper amount owed – is based on a strengthened commitment to treat taxpayers as customers. Doing this means that we will work hard to establish productive and positive relationships with all our customers and help them stay on track and voluntarily meet their tax obligations.

Our plan is the result of a year-long collaborative process that included our senior staff, several outside interest groups, agency partners, and an employee focus group. Our Mission and Vision statements highlight the importance we place on our knowledgeable and engaged employees as they continue to excel in giving their best for California taxpayers and achieving their fullest potential.

We are very aware of headlines today and the challenges that we may face in the future, yet our Strategic Plan looks forward to the future with optimism. We developed four goals together with strategies that are agile and built with flexibility to allow us to meet these challenges over the next five years. In addition, the plan brings out the

importance of our Enterprise Data to Revenue (EDR) project. This project is the largest in our history and will contribute in major ways to increase our efficiencies, service and enforcement goals.

We invite you to review our plan and contact our Planning, Performance, and Project Oversight Bureau with any questions at 916.845.3165.

---

## **Tax NewsFlashes**

We flashed this article on April 3:

### **IRS Penalty Relief to Farmers Affected by MF Global**

On March 23, 2012, IRS published [IR 2012-37](#) providing relief to farmers and fishermen affected by the MF Global bankruptcy. As an unusual circumstance, this relief is available through California's existing estimate tax waiver process as described below.

#### **Have not yet filed your return?**

To request a waiver of the estimated tax penalty, taxpayers who have not filed their returns, need to complete [Form 5805F](#). On line 16, state the reason for the waiver request is "MF Global." The form 5805F provides detailed instructions on how to complete line 16. Unlike federal, you may e-file your return.

**Important:** In order to process your return correctly, you *must* fill in the circle on Form 540, line 113; Long Form 540NR, line 123; or Form 541, line 42.

#### **Already filed your return**

To request a waiver of the estimated tax penalty if you have already filed your return, complete [Form 5805F](#), line 16, stating the reason for the waiver request is "MF Global." The form 5805F provides detailed instructions on how to complete line 16. You can fax your waiver request to 916.845.9300 or mail it to FRANCHISE TAX BOARD, PO BOX 942840 SACRAMENTO, CA 94240-0040.

We flashed this article on April 11:

## **CSEA Super Seminars 2012**

Register now for Super Seminar 2012 at [www.superseminar.org](http://www.superseminar.org)! CSEA's premier educational event is offered May 15 - 17 in Las Vegas, NV and May 31 - June 2 in Reno, NV!

We flashed this article on April 16:

## **Franchise Tax Board Updates Guidance on Real Estate Tax Deductions**

We issued new guidance to taxpayers who deduct real estate taxes on their state and federal returns.

The IRS recently issued [IRS Information Letter 2012-0018](#) providing further guidance in determining what a deductible real estate tax is. California tax law follows federal tax law in this area, which makes IRS guidance applicable for state tax purposes.

Real estate taxes based on the assessed value (ad valorem) of the property are generally deductible. The IRS information letter explains that contrary to information in its current forms and publications, assessments based on other than the assessed value of the property may be deductible in certain circumstances if they are levied:

- For the general public welfare.
- By a proper taxing authority.
- At a like rate.
- On owners of all properties in the taxing authority's jurisdiction.

However, amounts assessed only on specific properties for a local benefit (such as for streets, sidewalks, and like improvements) cannot be deducted as real property taxes. Taxpayers are permitted a deduction for the portion of the local benefit assessments that were imposed to repair, maintain, or meet interest charges for these local benefits.

In November 2011, we kicked off an education campaign to help taxpayers and tax preparers calculate the allowable real estate property tax deduction as an itemized deduction. As part of this effort and in response to some conflicting information regarding the deductibility of real estate taxes not assessed on an ad valorem basis, we wrote to the IRS Chief Counsel in December 2011 requesting clarification. The IRS Office of Chief Counsel issued a letter stating that there is no ad valorem requirement in the law regarding real estate tax deductibility and that certain portions of their current forms and instructions should be revised to more accurately reflect the IRS' position. To view a copy of our Chief Counsel's letter and the IRS' response, visit [ftb.ca.gov](http://ftb.ca.gov) and search for [real estate tax](#).

We removed the material that limits the deductibility of real estate taxes to those imposed on an ad valorem basis from our website. We are also revising tax form instructions to reflect this update. We will review the IRS' revisions to their forms and publications to provide comparable changes to California tax form instructions. We do not anticipate that these revisions will be made prior to the 2011 tax return due date.

At this time, we do not plan to add additional reporting requirements related to the real estate tax deduction beginning with the 2012 tax return.

---

## Ask the Advocate



### **When Does an Out-of-State California Business or Individual Need to File a California Income Tax Return?**

Sole proprietors and business entities, not based in California, still may be subject to California taxation if they are doing business in California or have income from California sources.

California Revenue and Taxation Code (R&TC) Section 23101 defines "doing business" as actively engaging in any transaction for the purpose of financial or pecuniary gain or profit. Unfortunately, this is often a facts and circumstance test. While we are able to discuss the facts and circumstances to consider in determining if an entity is doing business in California, taxpayers must ultimately decide if they are doing business in California.

R&TC Section 23101(b) does provide some "bright-line tests" for out-of-state business entities based on sales, property, and compensation. For tax years beginning on or after January 1, 2011, an out-of-state business entity that is not doing business under R&TC Section 23101(a) may be considered doing business in California under R&TC Section 23101(b) if it has sales, property, or payroll compensation in California in excess of "bright-line" threshold amounts. Sales, property, and compensation of the taxpayer include the taxpayer's pro rata or distributive share from pass-through entities.

See our March 2010 Tax News article, "[Doing Business in California](#)," and our May 2010, "[Ask the Advocate, Doing Business](#)," articles for more information, or search for "doing business" at [ftb.ca.gov](http://ftb.ca.gov).

For those unique circumstances where a taxpayer is unsure whether its activities constitute "doing business" in California under the general rule of 23101(a), the FTB will accept requests for written advice on that issue, but will continue to decline to rule on whether the specific factual threshold tests of R&TC Section 23101(b), have been met. See FTB Notice 2011-6.

Individuals, as well as sole proprietors and business entities may also need to file a California income tax return to report any income from California sources. The most common California income sources are:

- Gain from sale of real estate located in California.
- Income received through ownership of a partnership, S corporation, or limited liability company (LLC) that is doing business in California.

It is also common for nonresident individuals to have California source income from wages and salaries earned for services they perform while in California. [FTB Publication 1031](#), Guidelines for Determining Resident Status, provides more information.

California source income received through ownership of a partnership, S corporation or LLC doing business in California, is identified on the appropriate California Schedule K-1 issued by the entity.

For information about how non-California based business entities should report California source income received through ownership in another business, please see the instructions for the applicable booklet for the out-of-state entity and [Schedule R](#), Apportionment and Allocation of Income available online at [ftb.ca.gov](http://ftb.ca.gov).

Out-of-state sole proprietors and business entities are doing business in California or have income from California sources would need to file one of the following California income tax returns:

- Sole Proprietors file using [California Long Form 540NR](#) and provide a copy of Federal 1040 Return, including Schedule C.
- Partnerships, limited partnerships, and limited liability partnerships file using [California Form 565](#).
- Corporations file using either:
  - [California Form 100](#), if a C-Corporation
  - [California Form 100S](#), if an S-Corporation
- LLCs file using [California Form 568](#).
  - Exception: An out-of-state Limited Liability Company that only has California source income, but has not registered with the SOS and is not doing business in California files [California Form 565](#).

Certain nonresident individual owners of partnerships, S corporations, or LLCs may elect to file a group nonresident return using [Long Form 540NR](#). For more information, get [FTB Publication 1067](#), Guidelines for Filing a Group Form 540NR online at [ftb.ca.gov](http://ftb.ca.gov).

Individuals who do not live in California need to file a California Nonresident Income Tax Return when their worldwide total income or adjusted income exceeds limitations specific to their filing status. See [Form 540NR Booklet](#) for more information.

Partnerships, S corporations, and LLCs that are doing business in California are required to withhold income tax on certain payments to nonresident owners. To receive a refund of the withheld taxes, the nonresident owner must file a California income tax return to claim the refund even if they are not otherwise required to file a California income tax return.

Also, there may be filing requirements to for other California taxing agencies that have sales or employees located in California. Go to the BOE website at [boe.ca.gov](http://boe.ca.gov) for sales and use taxes, and the Employment Development Department's website, [edd.ca.gov](http://edd.ca.gov) for employment taxes.

**Steve Sims, EA**  
**Taxpayers' Rights Advocate**

*Follow me on Twitter at [twitter.com/FTBAdvocate](https://twitter.com/FTBAdvocate).*

---

## **Event Calendar**

As part of education and outreach to our tax professional community, we participate in many different presentations and fairs. We now provide a [combined-calendar](#) to show the events we are attending as well as other events happening with us such as interested party and board meetings.



## **Enterprise. Data. Revenue!**

---

### **EDR in the News**

#### **FIRM**

We recently rolled-out the Financial Institution Record Match (FIRM) program to conform to R&TC Sections [19266](#) and [19560.5](#). These statutes authorize us to implement a quarterly data match process to match our tax and non-tax debtor files against accounts held at financial institutions doing business in California. Financial institutions include banks, credit unions, insurance companies, brokerage companies, etc. This matching process provides us information about potential assets for collection purposes.

In April 2012, we kicked-off the first phase of the FIRM program. At that time, we notified approximately 180 financial institutions of their required participation in the FIRM program. On an ongoing basis we will notify additional financial institutions of their required participation.

---

### **Criminal Corner**

#### **Orinda Physician Arrested on State Income Tax Charges**

An Orinda physician was arrested April 4 on felony charges of state income tax evasion.

Coletta Marie Hargis, 56, is chief executive officer of Coletta M. Hargis, M.D., Inc. According to our special agents, Hargis allegedly received more than \$1.1 million in compensation for the years 2005 - 2010 and failed to file her personal income tax returns for these same years and her corporation's 2008 through 2010 tax returns. She faces six felony counts of tax evasion and six felony counts of deceptive conduct for the intentional concealment of income with the intent to evade tax. Each tax count carries a maximum sentence of three years in state prison.

Hargis owes the state more than \$91,000 in unpaid personal and franchise tax. Interest, penalties, and the cost of the investigation will be added to this figure and sought as restitution.

Hargis was booked into the Contra Costa County Detention Facility in Martinez. Bail is set at \$240,000 and her arraignment is not yet scheduled.

---

## **Big Business**

### **Legal Issues New Guidance**

In March, our legal division issued guidance on two important issues. The first, [Legal Division Guidance 2012-03-01, Federal Conformity](#), was intended to supersede Legal Division Guidance 2011-06-01, which was subsequently withdrawn by 2011-07-01. This guidance on the research and development credit answered the following questions:

1. Does California fully conform to the Internal Revenue Code section 41(c)(6) definition of "gross receipts" with respect to California service receipts?
2. Can a taxpayer with California Qualified Research Expenses and zero California Gross Receipts under RT&C Sections 17052.12, subdivision (g), paragraph (3), or Section 23609, subdivision (h), paragraph (3), claim the regular incremental Research and Development credit?
3. What does this mean for a taxpayer with California Qualified Research Expenses and Gross Receipts from the sale of tangible property, such as manufacturers?

The second, [Legal Division Guidance 2012-03-02 Large Corporate Understatement Penalty](#), answered the question "Can a taxpayer make a valid single sales factor (SSF) election and also report tax computed without the election in order to avoid the large corporate understatement penalty in the event the taxpayer is later determined to be ineligible to use the SSF formula?"

Our Legal Division routinely provides informal advice to external specialty publishers and non-legal staff in a form that is not generally reduced to formal written guidance such as technical advice memoranda or similar types of written guidance. It should be noted that items published under "Legal Division Guidance" are not considered "written advice" that may be relied upon within the meaning of RT&C Section 21012 and [FTB Notice 2009-09](#).