MARCH 1997

CALIFORNIA FRANCHISE TAX BOARD

Tax News

After the Tax Preparer Program: Business as Usual

When the new California Tax Education Council debuts on July 1, 1997, what's in store for tax preparers? The answer is: Business as usual, for the most part.

When the Department of Consumer Affairs shuts down its Tax Preparer Program at the end of June and the California Tax Education Council takes over (see "Tax Preparer Program to Shut Down" in the November 1996 Tax News), tax preparers may not notice the change-over.

Still in effect are the requirements that tax preparers complete 60 hours of tax instruction from an approved provider their first year and 20 hours a year thereafter, be at least 18 years of age and maintain a $5,000 surety bond.

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Spotting the Trends

Cartloads of tax returns from 1995 fill the foreground in this overhead photograph of the Franchise Tax Board's central office. The sampling of returns is used for revenue analysis and to identify economic trends.

Inside ...

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Tax News

Volume 97-2 March 1997

TAX NEWS is a bimonthly publication of the Accounts Receivable & Tax Policy Support Branch, California Franchise Tax Board. Its primary objective is to provide information to income tax preparers about state income tax laws, regulations, policies and procedures.

To update or correct your address or to subscribe to TAX NEWS (send $12 for a one-year subscription), write:
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or call: (916) 845-7070.

For information about California tax law and/or a client's account, contact:
Tax Practitioner Support Unit
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After the Tax Preparer Program: Business as Usual

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In terms of the educational requirement, tax preparers currently registered with the Tax Preparer Program have met the 60-hour course requirement and need only verify their Tax Preparer Program registration with the California Tax Education Council and complete the annual 20-hour continuing education requirement as they would have under Tax Preparer Program rules.

Instead of completing the training, obtaining a bond and then applying for registration with the Tax Preparer Program, individuals under the new program will complete the appropriate training, apply to the California Tax Education Council and receive certification of successful completion. They will use that certification when they apply for a bond. Once the bond is received, the individual can prepare returns in California.

Another change affects tax preparers who fail to perform their duties and are found guilty in court. Prevailing plaintiffs are entitled to reasonable attorney fees and costs, and tax preparers are subject to a $1,000 civil penalty.

The only new conditions concerning the bond requirement are that tax preparers:

- May not conduct business without a current bond.
- Must amend the bond within 30 days if any changes occur in their status.
- Must let customers know in writing that they maintain the bond and what the bond's number is. The written notice about the bond can be handed to customers or posted on the tax preparer's office wall.

The California Tax Education Council is made up of one representative from each qualifying professional society, association or other entity operating as a California nonprofit corporation and from each qualifying for-profit tax preparation corporation. So far, nine organizations are represented on the council (see box on this page).

Watch future issues of Tax News for more information on the California Tax Education Council and where to reach the council if you have questions. In the meantime, until July 1, 1997, the Department of Consumer Affairs' Tax Preparer Program will continue with its regular duties, which include handling tax preparer registrations and renewals, tax school approvals and taxpayer complaints. The Tax Preparer Program can be reached at (800) 952-5210.

(The Franchise Tax Board is not associated with either the current Tax Preparer Program or the upcoming program administered by the California Tax Education Council.)☐

Members of the California Tax Education Council

Currently, nine organizations are represented on the California Tax Education Council. They are:

- California Society of Accounting and Tax Professionals.
- California Society of Enrolled Agents.
- East Bay Association of Enrolled Agents, Inc.
- H&R Block, Inc.
- Inland Society of Tax Consultants, Inc.
- Jackson Hewitt Tax Service.
- Mission Society of Enrolled Agents.
- National Association of Enrolled Agents.
- National Association of Tax Practitioners.☐

Pointers for Partnership Returns

Advances in the Franchise Tax Board's processing capabilities mean that partnership returns are checked more thoroughly than before for accuracy and completeness.

To make sure that your partnership clients' returns are not delayed in processing, be sure to fill out Form 565, "Partnership Return of Income," accurately. So far, errors identified during processing show that tax professionals should pay close attention to these five points:

- The partnership's federal employer identification number (FEIN) must be valid. FEINs are issued, one to a customer, by the Internal Revenue Service. Be sure that you enter on line "D" the correct number exactly as the IRS assigned it.
- The partnership's exact legal name is required. If the legal name has changed since the partnership filed its last Form 565, check the box that has been added to the 1996 form for that purpose. If the name has not been changed legally but the partnership is doing business under a different name, enter the legal name on the "Partnership name" line and the name that the business uses in the "DBA" line.
- All *limited* partnerships that are registered in California must enter on line "H" their 10-digit Secretary of State file number.
- The number of Schedule K-1s attached to Form 565 must be the same as the number you enter on line "J."
- The information on the Schedule K-1s must reconcile with the return summary Schedule K (565).☐

New Publications Aid Schedule K-1 Filers

The Franchise Tax Board has two new publications to help partnerships file their Schedule K-1s (565) in efficient, paperless ways.

The free publications assist partnerships in filing on magnetic media and by an electronic data interchange (EDI). EDI is the computer-to-computer transfer of business information using standard national formats. Both filing methods alleviate the expenses associated with processing paper.

The new publications are:

"Guide for K-1 (565), Filing by Diskette or Magnetic Media," FTB Publication 1062. This guide includes the information needed to file California's Schedule K-1 (565) on magnetic media. It covers:

- Reporting requirements for partnerships planning to send California Schedule K-1s on magnetic media.
- Acceptable media formats.
- File specifications and filing procedures such as format reporting, test files, shipping instructions, the Form 565, "Partnership Return of Income," and payments.
- General record and K-1 record layout information.
- Information on penalties that may be assessed when a Form 565 is filed incorrectly.
- Numbers to call for more information or assistance.

"Guide for K-1 (565), Filing by EDI (Electronic Data Interchange)," FTB Publication 1062A. This manual tells partnership taxpayers how to implement EDI for filing California's Schedule K-1 returns. It provides, among other things, general EDI information, transmission process guidelines, communications requirements and tips on resolving problems.

Publication 1062 will be available this month, and Publication 1062A will be available in April. As soon as they are published, you can download them from FTB's *http://www.ftb.ca.gov* Internet address. Or contact the Tax Practitioner Support Unit by calling (916) 858-0571or faxing (916) 845-6377. You also may write Tax Forms Request, P.O. Box 307, Rancho Cordova, CA 95741-0307.☐

Inside ...

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President Designates Disaster Areas

What Is a Disaster Loss?

What constitutes a disaster loss?

A disaster loss is a casualty loss that is sustained as a result of a disaster and that is not reimbursed by insurance or otherwise.☐

By press time, the President had designated 48 California counties as disaster areas as a result of the storms and floods that occurred or began on December 28, 1996.

The designation allows storm and flood victims in the 48 counties (see page 5) to deduct their disaster losses on tax returns for either the year of the disaster or the previous year (see box below).

At press time, legislation had been proposed in California to allow amended returns to be filed by extended due dates. The Legislature also is considering a measure that would allow taxpayers in the disaster areas to carry over 100 percent of any excess disaster loss to future taxable years.

To amend a return, taxpayers must file a Form 540X, "Amended Individual Income Tax Return," or a Form 100X, "Amended Corporation Franchise or Income Tax Return."

Whether they deduct their loss on an original or an amended return, taxpayers must:

- Complete federal Form 4684, "Casualties and Thefts," using California amounts on the federal form, and attach it and any other supporting schedules to their return.
- Complete Form 4684, Section B, using California amounts, to figure the disaster loss for property that is trade or business, income-producing or rent or royalty property.
- Determine whether losses need to be reported on Schedule D-1, "Sales of Business Property," form FTB 3805V, "Net Operating Loss (NOL) Computation and NOL and Disaster Loss Limitation — Individuals, Estates and Trusts," or form FTB 3805Q, "Net Operating Loss (NOL)

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When to Claim Storm and Flood Losses

For personal income tax returns

Year of loss:	When to claim the loss:		
1996	**1995 return** On amended 1995 return due April 15, 1997. (Legislation could extend this date to October 15, 1997.)	**1996 return** On original 1996 return due October 15, 1997.	**1997 return** n/a
1997	n/a	On original 1996 return due October 15, 1997, or, if the return is already filed, on amended 1996 return due April 15, 1998.	On original 1997 return due October 15, 1998.

For corporate income tax returns

Follow the chart above, substituting "the 15th day of the third month after the close of the 1996 (or 1997) income year" for April 15, 1997, and April 15, 1998, respectively. Substitute "the 15th day of the tenth month after the close of the 1996 (or 1997) income year" for October 15, 1997, and October 15, 1998, respectively.

President Designates Disaster Areas

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Computation and NOL and Disaster Loss Limitations — Corporations."

- Attach to the return a statement that lists the disaster date and the city and county in which it occurred.
- Print "Disaster Floods '96/'97" in red ink at the top of Side 1 of the return. This will speed up the refund process.

For more information, see the free FTB Publication 1026N, "California Disaster Relief Tax Provisions." If you have Internet access, you may download, view and print the publication. It is available at FTB's *http://www.ftb.ca.gov* address.

You also may obtain a copy from FTB's Tax Practitioner Support Unit by calling (916) 858-0571 or faxing (916) 845-6377. Or write Tax Forms Request, Franchise Tax Board, P.O. Box 307, Rancho Cordova, CA 95741-0307.☐

Notices to Disaster Victims Delayed

During the December and January storms and floods in California, victims received many things, including donations of food, clothing and shelter. One thing they did *not* receive in the immediate aftermath of the storms and floods was a request from the Franchise Tax Board to file a delinquent tax return.

On an ongoing basis, FTB issues letters requesting either a delinquent tax return or substantiation that the individuals contacted had no requirement to file.

FTB computers that would have produced letters to 85,000 people, including many who were in designated disaster areas, were reprogrammed to delay the notices. Another 5,000 letters already produced were retrieved from the FTB mail room for distribution at a later date.

In addition, a number of Notices of Proposed Assessment were delayed.☐

Forty-eight Counties Named Disaster Areas

At press time, the 48 counties designated disaster areas by the President as a result of the 1996-97 storms and floods are: Alameda, Alpine, Amador, Butte, Calaveras, Colusa, Contra Costa, Del Norte, El Dorado, Fresno, Glenn, Humboldt, Kings, Lake, Lassen, Madera, Marin, Mariposa, Mendocino, Merced, Modoc, Mono, Monterey, Napa, Nevada, Placer, Plumas, Sacramento, San Benito, San Francisco, San Joaquin, San Luis Obispo, San Mateo, Santa Clara, Santa Cruz, Shasta, Sierra, Siskiyou, Solano, Sonoma, Stanislaus, Sutter, Tehama, Trinity, Tuolumne, Tulare, Yolo and Yuba.

Victims who incur losses in disaster areas designated by the President qualify to claim the losses on prior year tax returns (see article on page 4). ☐

Need to Replace Tax Return Lost in Flood?

Your clients who need to replace tax returns that were lost or destroyed during the December storms and January floods in Northern California can obtain them from the Franchise Tax Board at no cost.

Clients seeking replacement tax returns should write to RID Unit, Franchise Tax Board, P.O. Box 942840, Sacramento, CA 94249-0060. Or they can complete form FTB 3516, "Request for Copy of Tax Return."

Form FTB 3516 is available in the 1996 Package X. If you have Internet access, you can view, download and print the form from FTB's *http://www.ftb.ca.gov* address. Or you can write Tax Forms Request, P.O. Box 307, Rancho Cordova, CA 95741-0307.

Storm and flood victims will not be charged for copies of their tax returns if "Disaster Floods '96/'97" is printed at the top of the letter or form. For other taxpayers, the charge for a copy of a tax return is $10.☐

FTB Calendar

March

- Taxpayer Services Center and Tax Practitioner Support Unit telephone service is available from 7:00 a.m. to 8:00 p.m. through April 15.
- Notices of Proposed Assessment mailed to individuals who failed to file 1995 returns.
- Package X CD-ROM update mailed.

20 Previous month withholding at source payments due if total withholding exceeded $2,500.

April

5 Taxpayer Services Center and Tax Practitioner Support Unit telephone service is available this Saturday.

12 Same as above.

15 First 1997 personal income tax estimate payments due.

15 Personal income tax returns due.

16 Taxpayer Services Center and Tax Practitioner Support Unit telephone service resumes normal business hours of 8:00 a.m. to 5:00 p.m.

20 See March 20.

26 Small Business Fair, Hayward.

May

15 Homeowner/Renter Assistance filing season begins.

20 See March 20.

June

17 Personal income tax estimate payments due.

20 See March 20.☐

Small Business Fair Offers One-Stop Shopping

A Small Business Fair in Hayward can be a valuable one-stop source of information for people who own or want to own small firms.

In one day, at one place, your San Francisco Bay Area clients can learn how to start a new business, write a business plan, avoid penalties and determine whether they are considered employers. They also will find out when to pay sales taxes and which tax and other forms they must file.

The Hayward Small Business Fair is scheduled for April 26 from 8:30 a.m. to 3:00 p.m. The event will be held in the University Union Building, 25800 Carlos Bee Boulevard, California State University, Hayward.

One of the fair's highlights is a series of 10 seminars and workshops covering such topics as business taxes, employees and independent contractors, employment eligibility, forms of business ownership, insurance issues, sales and use tax exemptions, success stories and what nonprofits can offer small business owners.

In addition, people attending the Small Business Fair can pick up free information in an exhibit area and meet with representatives of government agencies and nonprofit organizations.

Participants include the Alameda County Assessor's Office, Bay Area Entrepreneur Association, Board of Equalization, California Chamber of Commerce, Community and Economic Services of the City of Hayward, Consumer Credit Counseling Service, Department of Trade and Commerce, Division of Labor Standards Enforcement, East Bay Small Business Development Center, Employment Development Department, Federal Trade Commission, Franchise Tax Board, Hayward Chamber of Commerce, Hayward Public Library, Immigration & Naturalization Service, Internal Revenue Service, Private Industry Council, San Mateo County Assessor's Office, Small Business Administration, State Compensation Insurance Fund and U.S. Postal Service.☐

Phone for Small Business Fair Information

For more information on the Small Business Fair in Hayward, contact the State Board of Equalization at one of three locations.

Call (415) 396-9800 in San Francisco, (510) 286-0347 in the East Bay and (408) 277-1231 in the South Bay.☐

Tax Talk Expands into Video Series

The producers of Tax Talk, the annual seminar telecast live to 20-plus locations in California, Nevada and Oregon, will introduce a video series in 1997.

The videos, which will update material covered at Tax Talk seminars in the past, will be packaged with exercises and a test. Individuals who successfully complete the test will be entitled to three continuing education credits. Each video will cover one topic.

The videos are the third variation on the Tax Talk theme, joining the annual seminar and a home study course based on each seminar.

Watch upcoming issues of Tax News for information on when the Tax Talk videos will be available for purchase.

Tax Talk is a program of the Center for Tax Education presented by the Franchise Tax Board, Employment Development Department, Internal Revenue Service, State Board of Education and the School of Business Administration, California State University, Sacramento.☐

Legislation to Watch

California legislators are considering measures on the following topics of interest to tax professionals:

Age 65 exemption credit. SB 140 (McPherson) would temporarily suspend the annual inflation adjustment to the exemption credit for an individual 65 years of age or older. The adjustment would be suspended for taxable years beginning on or after January 1, 1997, and ending before January 1, 2002. The resulting revenue savings would be transferred to the California Seniors Special Fund. The bill also would extend the operative date of the California Fund for Senior Citizens, a designated voluntary contribution on the individual tax return, until January 1, 2002.

Agriculture credit. SB 38 (Johannessen) would create a tax credit equal to 6 percent of the cost paid for specified tangible personal property and capitalized labor costs used by taxpayers involved in agricultural operations.

This credit is modeled after the Manufacturers' Investment Credit and contains many similar provisions and definitions. Some of the similar provisions deal with binding contracts and leased property; others allow small businesses a longer carryover period and require recapture of the credit if the property is removed from the state or no longer used for agricultural purposes.

The credit would be allowed for taxable and income years beginning on or after January 1, 1998, and would cease on January 1, 2005. However, the credit could first be claimed on 1999 income tax returns.

Business registrations. AB 61 (Strom-Martin) would require the Secretary of State to adopt by July 1, 1998, regulations to allow businesses to register at a single location for all state and local agencies. The businesses would receive a statewide fictitious business name that would be accepted by all agencies and an account number that would be used by the Secretary of State, the Board of Equalization and the Employment Development Department. The bill also would require access to the registry either through a toll-free telephone number or electronically.

Capital gain exclusion. AB 9 (Campbell) would exclude from gross income 100 percent of any gain from the sale or exchange of a "California capital asset," which would be defined as tangible property located in this state or an ownership interest in a California-based company. The bill would apply to taxable and income years beginning on or after January 1, 1997.

Capital losses. SB 100 (Lewis) would allow a deduction for any loss from the sale or exchange of a taxpayer's principal residence. The residence would have to be located in California and used by the taxpayer for 24 consecutive months before the sale or exchange. The loss deduction would be limited to $250,000, but the allowable deduction in any one tax year would be subject to the capital loss rules under the Internal Revenue Code. As a result, the loss would be allowed to the extent of capital gains plus $3,000. Any remaining loss would be carried over to succeeding years until it was exhausted. The bill would apply to contracts for sales or exchanges entered into on or after July 1, 1997. It would not apply to any individual who fails to file an income tax return for the year of the loss.

Disaster losses. AB 1X (Cardoza, et al.), AB 94 (Cardoza) and AB 4X and AB 91 (Bowler) would add to existing disaster relief provisions of the Personal Income Tax Law and the Bank and Corporation Tax Law losses due to storms or flooding that occurred in 1996 or 1997 in any county declared a disaster area. As a result, if a loss exceeds income for the year it is claimed, the taxpayer would be able to carry forward for five years 100 percent of the excess. The taxpayer also would be able to carry forward for the next 10 years 50 percent of any disaster loss remaining after the five-year period.

SB 1X (Leslie) is a similar bill but, unlike the above measures, covers storms or flooding occurring only in December 1996 or January 1997, not throughout both years.

Earned income credit. SB 43 (Solis) would create a tax credit of an unspecified percentage based on the federal earned income credit. The

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Where to Get Copy of Legislative Bill

Do you want more information on one of the legislative measures covered in the article on this page? If so, you can obtain a copy of any bill from:

Legislative Bill Room
Room B-32
State Capitol
Sacramento, CA 95814
(916) 445-2323.☐

SBE Opinions

Appeal of AeroVironment, Inc., November 15, 1996 (Opinion adopted January 10, 1997). According to the terms of former Revenue and Taxation Section 23601, the solar energy credit could be claimed only by the entity that was the "owner" of the property upon which the qualifying energy-saving device has been constructed. Thus, the solar energy credit could not be claimed at the unitary group level.☐

Legislation to Watch

CONTINUED FROM PAGE 7

Franchise Tax Board would be required to provide training and information to employers so that employees who are eligible for the credit may adjust their withholding allowances to reflect the credit. The credit would be allowed for taxable years beginning on or after January 1, 1997, and could be carried over indefinitely. AB 83 (Villaraigosa) contains similar provisions.

Education trust. AB 13 (Firestone) would create the California Postsecondary Educational Scholarshare Trust. Participants would be allowed to invest money in the trust for the benefit of a specific beneficiary who may be designated from the date of birth through age 14. Payments from the trust would begin the first full academic semester after the beneficiary's 17th birthday. The trust, income from its operations and interest earned on money paid by a participant would be exempt from state taxation. The bill would become operative on January 1, 1998.

Employers' school facility credit. AB 56 (Mazzoni) would create a tax credit equal to 30 percent of the taxpayer's expenses paid or incurred during the taxable or income year for establishing a school facility to be used by the children of the taxpayer's employees, children of the taxpayer's tenants' employees or children in the same district. The credit amount would be limited to $50,000 for any taxable year, and any excess could be carried over. The credit would apply to taxable or income years beginning on or after January 1, 1997, and before January 1, 2007.

LAMBRAs. AB 3 (Baca) would direct the Trade and Commerce Agency to allow an additional six months for the competition period for designating Local Agency Military Base Recovery Areas (LAMBRAs).

LARZ. Two bills are of interest to companies operating in the Los Angeles Revitalization Zone (LARZ). AB 69 (Washington) would extend the sunset of the LARZ sales or use tax credit from taxable years beginning before January 1, 1998, to taxable years beginning before January 1, 2001, for taxpayers who file under the Personal Income Tax Law. This bill does not extend the sunset date for the LARZ.

AB 82 (Villaraigosa) would extend the sunset of the LARZ sales or use tax credit from taxable or income years beginning before January 1, 1998, to taxable or income years beginning before January 1, 2003, for taxpayers who file under either the Personal Income Tax Law or the Bank and Corporation Tax Law. This bill also would extend the operation of the LARZ Act under the Government Code by extending the repeal date of the applicable chapter from December 1, 1998, to December 1, 2003.

Legislation analysis. SB 58 (Ayala) would require every state agency to analyze any legislative measure that might significantly affect it. The agencies would be required to deliver their analyses to the bill's author and appropriate policy committee no later than seven calendar days before the bill's first hearing.

Low income credit. SB 83 (McPherson) would create a tax credit, ranging in amount from 20 to 100 percent of net tax, for low-income individuals. The credit would be based on both the individual's adjusted gross income and filing status. The credit would be allowed against "net tax" after all other credits have been claimed. The adjusted gross income amounts used to determine the applicable credit percentage would be adjusted annually for inflation. The credit could not be claimed by trusts, estates or taxpayers who pay alternative minimum tax. The credit would be available for taxable years beginning on or after January 1, 1997, and before January 1, 2001.

Minimum franchise tax. Two measures address the minimum franchise tax. AB 8 (Brewer and Leach) would eliminate the minimum franchise tax for the first five income years of operation for any bank or corporation that forms on or after January 1, 1997, and that does not have positive net income. The bill would not apply to specified entities, such as limited partnerships and limited liability

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Legislation to Watch

Continued from page 8

companies, or to any bank or corporation that reorganizes solely for the purpose of reducing its minimum franchise tax. The bill also would specify that the existing exclusion from the minimum franchise tax for certain domestic banks or domestic corporations that have filed a certificate of dissolution applies only to those entities with gross receipts of $10 million or less.

AB 27 (Strom-Martin) would reduce the initial minimum franchise tax from $600 to $300 for qualified new corporations as defined by existing law. However, if the corporation's gross receipts exceed $1 million or its measured tax exceeds $800, the corporation would be liable for an additional tax of $500 on the due date of its franchise tax return. This bill would apply to income years beginning on or after January 1, 1998.

Open meetings/teleconferences. SB 95 (Ayala) would make several changes to the Bagley-Keene Open Meeting Act. The changes include, but are not limited to, requiring a state body such as the Franchise Tax Board to list, with a brief general description on an open meeting agenda, all items for discussion in a closed meeting and to report orally or in writing in open session any action taken in closed session. The bill also would extend from January 1, 1998, to January 1, 2001, the sunset date of the existing law that allows state agencies to teleconference. And it would limit a state entity's teleconferencing discussions to public comment or testimony and to the entity's deliberations.

Residential roof credit. AB 77 (Morrow) would create, under the Personal Income Tax Law and the Bank and Corporation Tax Law, a tax credit equal to an unspecified percentage of the costs for replacing a residential wood shake roof with a new roof of fire-resistant materials. The credit amount caps at $5,000. The credit would be allowed for taxable or income years beginning on or after January 1, 1997, and may be carried over until it is exhausted.

A second bill, AB 109 (Kaloogian), would provide a tax deduction for the qualified cost of replacing a nonfire retardant roof on a residential dwelling in California with a fire retardant one. The qualified cost would be the excess cost, including materials and labor, of the fire retardant roof over the nonfire retardant roof.

S corporations. SB 5 (Lockyer) would substantially conform California law to the changes made to federal S corporation tax law by the Small Business Job Protection Act of 1996. It generally would conform to 16 federal items including increasing from 35 to 75 the maximum number of shareholders an S corporation can have, allowing trusts and certain financials to be S corporation shareholders and allowing S corporations to hold subsidiaries.

The bill would raise the current state S corportion tax of 1.5 percent. The tax rate would be changed for income years beginning on or after January 1 for each of the following years: 1997, 1.6 percent; 1998, 1.65 percent; 1999, 1.7 percent; 2000 and thereafter, 1.6 percent.

In addition, the bill has one transitional provision for electing S corporations that allows estimate tax payments made while a C corporation to be transferred to the individual shareholders' tax accounts. The transitional provision would be effective only for S corporation elections made for income years beginning in 1997.

Small business expensing. Under the Personal Income Tax Law, AB 41 (Murray) would conform state laws regarding small business expensing to current federal law, increasing the amount of tangible property a small business may elect to treat as a expense in the year acquired from $12,500 to $18,000 in 1997, from $15,000 to $18,000 in 1998, to $19,000 in 1999, to $20,000 in 2000, to $24,000 in 2001 and 2002 and to $25,000 in 2003.

Solar energy credit. Under the Personal Income Tax Law and the Bank and Corporation Tax Law, SB 116 (Peace) would create a tax credit for solar energy devices installed on premises that the

Continued on page 12

Assessments Proposed for 120,000

The Franchise Tax Board is sending Notices of Proposed Assessment this month to 120,000 individuals for failing to file 1995 tax returns.

Previously, these individuals received a letter from FTB stating that information from various sources indicated that they are required to file a tax return. Because they did not respond by either filing a return or showing why they are not required to do so, assessments are now proposed.

The proposed assessments include not only tax due, based on available information, but penalties, interest and a fee to cover the cost of enforcing the filing requirement.☐

Remind Electronic Filers to Pay Balance Due

When a tax return goes over the wire, any balance due payments must go in the mail.

Remind your clients that filing tax returns electronically is not the end of the process when they have a tax liability. The tax they owe must be paid in full by April 15, 1997, in order to avoid penalties, interest charges and correspondence from the Franchise Tax Board.

Clients should send their payments with form FTB 3582, "Payment Voucher for Electronically Transmitted Returns." ☐

Electronic Filing: Good for Business

Do you like keeping a step ahead of the competition? If so, offer your clients the option of filing their California tax returns electronically.

Electronic filing can be a better way to do business for you and your clients because it provides fast refunds and is completely paperless. And you can be confident that FTB receives your clients' returns because you will receive an acknowledgment right away.

This year, you can file 540, 540A and 540EZ returns electronically whether your clients will receive a refund, have a balance due or have no balance due. FTB will accept electronically filed returns through October 15, 1997.

If you have questions about the electronic filing program or would like to apply to file electronically, call FTB's Electronic Filing Help Desk at (916) 845-0353 or fax (916) 845-5340. Staff is available to help you on weekdays from 8:00 a.m. to 5:00 p.m.☐

1997 Electronic Filing Calendar

If you plan to file any clients' California returns electronically this year, here are the dates to remember:

- **April 15 -** Last day to pay on time for a balance due return.
- **April 30 -** Last day that the Franchise Tax Board accepts test transmissions.
- **October 15 -** Last day to file an electronic return.
- **October 18 -** Last day to retransmit a rejected return.☐

Electronic Filing Is on the Rise

Increased numbers of taxpayers are using California's electronic filing system.

As of February 17, 1997, 145,302 people had filed their tax returns electronically. On the same date last year, 104,324 had filed electronically.

Close to 84,000 of the electronically filed returns were Forms 540A. Almost 45,000 were Forms 540, and nearly 17,000 were Forms 540EZ. Additional Form 540EZ taxpayers filed their returns this year by telephone (see "TeleFilers Ring in the New Year" on page 14).☐

Make Revisions to 1996 Forms

The Franchise Tax Board has revised five 1996 tax forms.

If you are using any of the following forms, be sure to make the necessary revisions on the forms:

Form 100, "California Corporation Franchise or Income Tax Return."

Side 3, Schedule H, column (j) reads: "Allowable...(Side 1, line 11)." It should read: **"<u>Allowable...(Side 1, line 10</u>)."**

Side 3, Schedule H, "Total" line reads: "Total. Add columns (f), (h) and (j). Enter here..." It should read: **"<u>Total. Enter here....</u>"**

Form 540NR, "California Nonresident or Part-Year Resident Income Tax Return."

Instructions, Page 2, "What's New for 1996," should read: **<u>"PENSION INCOME OF RETIREES WHO MOVE TO ANOTHER STATE. California incorporated the federal preemption regarding the taxation of nonresident pension income (Public Law 104-95). Payments based on California service and received by nonresidents on or after January 1, 1996, are not taxable to California. If California state income tax was</u>**

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Where to Get a Package X

Do you need a Package X?

To order either a bound or loose-leaf paper version or a CD-ROM version of the California Package X, call (916) 845-7070 for an order form. When you receive the order form, send it with a check or money order to the address on the form. Paper Package Xs are $12; the CD-ROM, which includes 1996, 1995 and 1994 California tax forms and 1996 Internal Revenue Service Package X forms, is $19.

If you need California tax forms in a hurry, you can find them on the Internet. To download the forms, go to the Franchise Tax Board's *http://www.ftb.ca.gov* address. In addition, some libraries and quick-print shops stock the California Package X so that you can photocopy the forms you need.☐

Package X: CD-ROM Orders Increase

Tax practitioners are ordering more than twice as many Package Xs in a CD-ROM format than they did last year.

Almost four months after distributing Package X order forms, requests for the CD-ROM version of the Package X hit more than 5,900. Last year, approximately 2,500 CD-ROMs were ordered over a 12-month period.

Like last year, requests for paper versions of the Package X continue to exceed requests for the CD-ROM. Tax professionals have ordered close to 30,000 books so far this year. The figure is lower than last year's due to increasing CD-ROM sales and possibly also to the availability of Package X tax forms on the Internet.☐

Make Revisions to 1996 Forms

Continued from page 10

<u>withheld from your payments, file Form 540NR for a refund."</u>

Form 568, "Limited Liability Return of Income."

Instructions, Page 4, "When and Where to File," reads: "Mail Form 568 to:..." It should read: **<u>"Mail Form 568 With Payment to:...and Mail Form 568 Without Payment to:</u>**

FRANCHISE TAX BOARD
PO BOX 942857
Sacramento CA 94257-0600."

FTB 3510, "Credit for Prior Year Alternative Minimum Tax - Individuals and Fiduciaries."

Instructions, Side 2, 3rd column, Line 24, 3 bulleted items reads: "Schedule P (540), Part V,...column (d); Schedule P (540NR), Part VI,...column (d); Schedule P (541), Part V,...column (d);" It should read: **<u>"Schedule P (540), Part V,...column b; Schedule P (540NR), Part VI,...column (b); Schedule P (541), Part V,...column (b);...."</u>**

Schedule H (100S), "S Corporation Dividend Income."

"Total" line reads: "Total. Add column (f) and column (g). Enter here..." It should read: **<u>"Total. Enter here...."</u>**

FTB 5806, "Underpayment of Estimated Tax by Corporations."

Side 1, Part I, Line 6c: Line 6c should be deleted.

Side 1, Part I, Line 7 reads: "Subtract line 6c from the sum of line 6a and line 6b." It should read: **"<u>Add line 6a and line 6b.</u>"**

FTB 5806, "Underpayment of Estimated Tax by Corporations."

Instructions, Page 1, Part I, 3rd column after Line 6a should read: **"<u>Line 6b - Enter the overpayment from the previous installment. However, if an underpayment existed on any prior installment, pay that underpayment first.</u>"**

Package X on CD-ROM Is Updated

All tax preparers who ordered a Package X on CD-ROM this year are entitled to a second disk with updated information.

Distribution of the updated CD-ROMs by first class mail began early this month, so you may already have received your copy.

The second CD-ROM includes any necessary clarifications to tax forms identified since the Package X was published in December. It is included in the purchase price.☐

Quick Collect Payment Fee Increases

The cost of making a same-day payment of an outstanding California tax liability by Western Union is now one dollar more.

The flat fee for Western Union's Quick Collect program increased from $10.50 to $11.50 on January 1, 1997. With Quick Collect, taxpayers can immediately transfer money to the Franchise Tax Board to pay a tax obligation.

The $11.50 fee covers one Quick Collect payment of $5,000 or less. Any amount more than $5,000 requires a second money transfer with an additional $11.50 fee.

Quick Collect was introduced as a tax payment option through a pilot program in 1992. The next year, it became an ongoing program.☐

Keep Tax News Coming

Is your subscription to Tax News about to run out? If so, you will receive a notice by mail.

To keep Tax News coming, be sure to return the notice and your check for another year's subscription to the newsletter.☐

Dronenburg Is Franchise Tax Board Member

As the new chair of the State Board of Equalization, Ernest J. Dronenburg, Jr. now serves on the three-member California Franchise Tax Board.

Dronenburg joins continuing board members Controller Kathleen Connell, who is the board's chair, and Department of Finance Director Craig L. Brown.

Dronenburg is serving his fifth term on the Board of Equalization. He was a member of the Franchise Tax Board on four previous occasions. He also was the architect and key sponsor of the California Taxpayers' Bill of Rights, which became law in 1989.☐

Legislation to Watch

CONTINUED FROM PAGE 9

taxpayer owned in California during taxable and income years beginning on or after January 1, 1997, and before January 1, 2007. The credit would be 25 percent of the cost of the solar energy system up to a $1,000 maximum credit. Any unused credit would be carried forward to reduce tax liability for five years.

Trial jury compensation credit. SB 14 (Calderon) would establish a tax credit for employers equal to an unspecified percentage of compensation paid to an employee serving on a trial jury. Any excess credit could be carried over until it is exhausted. The credit would be allowed for taxable and income years beginning on or after January 1, 1998.

Voluntary contributions. SB 78 (Thompson) would reenact the Endangered and Rare Fish, Wildlife and Plant Species Conservation and Enhancement voluntary contribution, which was repealed on January 1, 1997. The language duplicates the existing statute except that the new repeal date would be January 1, 2002. Therefore, the bill would allow the Endangered and Rare Fish voluntary contribution to remain on 1997 through 2001 income tax returns.☐

The Question Column

How Do Other States Collect Taxes Here?

Some states assess California residents and partnerships doing business in their states for taxes on income purported to be earned in those states.

- **Does California have agreements and an obligation to assist other states in collecting taxes assessed against California residents?**
- **What procedures do other states have to follow to collect taxes here?**
- **Does California benefit from assisting other states?**

California does not have any agreements with or obligations to other states to assist them in collecting taxes from California residents. However, California may enter into an information exchange agreement with another state to provide it with information on a taxpayer.

Before another state may take involuntary collection actions in California, it must file a civil judgment within California. The other state also may hire an agent operating in California to attempt to collect on the liability.

California benefits from the information agreements it has with other states because the information often helps the Franchise Tax Board locate debtors and their assets and is also useful in conducting audits. The information agreements have strict provisions to maintain the security of the shared information.

What Attaches to State Return?

When a copy of the federal return must be attached to a California individual tax return, should the taxpayer include Form 5471, "Information Return of U.S. Persons With Respect to Certain Foreign Corporations," that was filed with the federal return?

Yes. Whenever a taxpayer is required to attach a copy of the federal Form 1040 to

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The Question Column

CONTINUED FROM PAGE 12

the California return, all supporting federal forms and schedules should be included.

Who Qualifies for Head of Household Status?

To qualify for the head of household filing status, a taxpayer must maintain his or her home as the principal place of abode for his or her child for more than one-half of the tax year. Must the one-half of the taxable year consist of consecutive days if the number of days totals more than 183? For example, a child lived with its father in the father's home for 189 days. From January through August, the child lived in the father's home every other weekend, one day during the week and one entire week. From September through December, the child lived in the father's home full time except for one weekend each month. Does the father qualify for head of household filing status?

Assuming that the father met all of the other requirements for the head of household filing status, the answer depends on who had physical custody of the child during the year.

If the mother had primary physical custody during the first eight months and the father had visitation every other weekend, one day a week and one entire week and if beginning in September the father had primary physical custody and the mother had visitation one weekend per month, the father would not qualify for the head of household filing status. The father's home would not be considered the child's principal place of abode until September, when the father had primary physical custody and the child lived with the father. Because the father’s home was not the child’s principal place of abode for more than one-half of the year, the father would not qualify for the head of household status.

If the parents had joint physical custody of the child and the father's custody time was every other weekend, one day a week and one entire week for the first eight months and full time, except for one weekend a month, thereafter, the father’s home would be the child’s principal place of abode for more than one-half of the year. As a result, the father would qualify for the head of household filing status.

Each parent is considered to have maintained a principal place of abode for the child during the periods of their physical custody. The parent who had physical custody for more than one-half the year would qualify for the head of household status.

Divorcing Couples: Who Gets Tax Overpayment?

A couple that has been filing California tax returns using the "married filing joint" status gets or files for a divorce and changes filing status to either "single" or "married filing separate." The couple's last "married filing joint" return reflects a tax overpayment to be applied to the next year's estimated taxes. To whose estimated taxes is the overpayment applied?

In this situation, the full amount of all payments is applied to the next year's estimated taxes of the first former spouse to file a return unless the taxpayers indicate otherwise. For a couple that agrees to split the payments under a different arrangement, Form 540, line 39 instructions state: "If you and your spouse paid joint estimate tax but are now filing separate returns, either of you may claim all or part of the amount paid. Attach a statement signed by you and your spouse explaining how you want your payment divided."

Attaching a statement is not required by law. However, a notation near line 39 on Form 540 will help assure that the credit is handled according to the taxpayers' wishes.☐

Do You Have a Question?

Would you like your question answered in The Question Column?

To submit a question to the column, write to: Editor, Tax News, P. O. Box 520, Rancho Cordova, CA 95741-0520.☐

Withholding Verification Spots Federal Amounts on California Returns

Reporting federal withholding amounts on California tax returns is the first trend in taxpayer errors spotted by the Franchise Tax Board's new automated withholding verification process.

Since January 1997, withholding amounts have been verified on-line, thanks to an automated information exchange between FTB and the Employment Development Department. The exchange is part of an ongoing integration of California's personal income tax and employment tax systems.

The erroneous withholding amounts are occurring primarily on tax returns filed through FTB's TeleFile system (see "TeleFilers Ring in the New Year" on this page). Because returns that are filed by telephone are not accompanied by W-2 and other forms as paper tax returns are, FTB staff uses its new database to resolve incorrect information provided by TeleFilers. Where EDD and tax return data do not match, FTB staff may contact employers to verify the information on returns that claimed high withholding amounts.

When errors are identified, FTB informs the taxpayers in question that the withholding amounts have been corrected.

The taxpayers are not required to file amended returns. Before the FTB/EDD automated information exchange was instituted, withholding amounts were verified manually as returns were processed. Amended returns sometimes were filed in cases of errors.

For more information on the automated withholding verification process, see the November 1996 and January 1997 issues of Tax News. And watch upcoming issues for filing season statistics.☐

Withhold at Source Phone Service Improved

The Franchise Tax Board has improved its telephone service for callers with withhold at source questions.

"Withhold at source" refers to withholding that is required when a nonresident individual or a corporation or partnership not qualified to do business in California or without a permanent place of business here receives payments of California source income.

Starting now, FTB's withhold at source telephone number will connect callers with an interactive voice response (IVR) system. The system provides callers with quick, automated responses to frequently asked questions in addition to fast access to the withhold at source representative most qualified to address their needs.

The withhold at source IVR telephone number is (916) 845-4900.☐

Need a Speaker?

If your tax practitioner organization or community group would like to hear about tax law or tax issues at an upcoming meeting, call the Franchise Tax Board for a speaker.

You can reach FTB's Speakers' Bureau at (916) 845-5257. Be sure to call at least four weeks before the event for which you need a speaker.☐

TeleFilers Ring in the New Year

Fifty people started the first business day of the new year by filing their California income taxes by telephone.

The early filers are among the 115,187 taxpayers who had participated in the Franchise Tax Board's TeleFile program by press time. At the same time last year, only 6,276 individuals had used the TeleFile program; however, relatively few individuals were invited to participate last year.

Approximately 240,000 taxpayers are expected to file their tax returns by telephone this year. They represent 15 percent of the 1.6 million taxpayers who received FTB's TeleFile booklet because they appear to qualify for the program.

Last year, when the program was launched, only 100,000 taxpayers were invited to participate. This year, in addition to sending the TeleFile booklet to more taxpayers, FTB has produced print and movie theater advertisements for the program, encouraged press coverage, set up college campus TeleFile sites and joined the Internal Revenue Service in promoting the TeleFile program.☐

State Disability Insurance Credit Refunds Issued

Taxpayers who qualified for state disability insurance (SDI) credits during the last three tax years but did not claim them will be receiving refunds.

Senate Bill 1682 - Johnston (Ch. 96-1157) provides that taxpayers entitled to the SDI credit for 1993, 1994 or 1995 will receive refunds. Separate checks will be issued for each year.

Until the 1996 tax year, only California Forms 540 and 540NR featured a place to claim a credit for excess SDI that was withheld. Taxpayers who filed Forms 540A or 540EZ may not have been aware of the credit because, although instructions were provided to claim the credit, there was no place to claim it on those forms.

The Franchise Tax Board and the Employment Development Department have been working together to identify these taxpayers and issue the refunds. The agencies also are working to identify and issue refunds to taxpayers who filed Forms 540 and 540NR for the same years and qualified for the credit but did not claim it. However, according to law, only Form 540A and 540EZ filers are entitled to interest, which runs from the original due date of the return.

To qualify for a refund of excess SDI withheld, a taxpayer must have:

- Worked for two or more employers during the tax year.
- Received more than $31,767 in wages from the two or more employers.
- Attached a copy of a W-2 form from each employer showing the amount of SDI withheld.
- Had more than $412.97 withheld from all employers for tax years 1993 and 1994 or more than $317.67 withheld for tax year 1995.

The first refunds were issued in late January 1997 with an explanatory notice. SB 1682 requires that all of the refunds be issued by October 15, 1997.

Taxpayers do not need to call FTB or EDD. FTB will issue refunds to all taxpayers who qualify.□

Pushing the Envelope

The Franchise Tax Board receives mail by the cartful. As one staff member unloads envelopes, another prepares to feed them into machinery that opens 18,000 envelopes per hour.

Substitute Forms Released Before Approval

In February, the Franchise Tax Board learned that substitute/scannable tax forms developed by T. K. Publishing, Inc. (Tax Shop) were released to the public before receiving FTB approval. Subsequently, the company submitted its substitute/scannable tax forms and, after making adjustments, received approval.

If you purchased tax forms or software from T.K. Publishing before January 23, you may want to ask the firm if you have the approved software.

Tax preparers should be sure to use tax software and computerized processing services that produce FTB-approved forms. To verify that you are using such forms, ask your software company for a copy of the FTB approval letter for the tax forms you need.□

Reminder: Hotline Has New Name

The Franchise Tax Board's Tax Practitioner Support Unit is the new name for the Tax Practitioner Hotline and for Tax Practitioner Electronic Correspondence.

To reach the Support Unit by telephone, call (916) 845-0571. Or send a fax to (916) 845-6377.

Both the telephone and fax numbers are intended for tax practitioners only, not for their clients.☐

Use Revised 100X to Amend Corporate Return

When you amend tax returns for your corporate clients for 1988 and later tax years, be sure to use the current version of the correct form.

To avoid substantial delays in the processing of your clients' tax forms, use the version of California Form 100X, "Amended Corporation Franchise or Income Tax Return," that has a three-column format.

The three-column form, developed in 1993, breaks the "Income and Deductions" and "Computation of Tax" sections of the return into three columns: "As originally reported or as adjusted," "Net change" and "Correct amount." The Form 100X that featured only one column for entering figures is now obsolete.

The current Form 100X is included in the 1996 Package X. If you have Internet access, you may download, view and print the form from the Franchise Tax Board's *http://www.ftb.ca.gov* address. You also may order the form from FTB's F.A.S.T. (Fast Answers about State Taxes) system by calling (800) 338-0505. Or write Tax Forms Request, P.O. Box 307, Rancho Cordova, CA 95741-0307.☐