

Tax Return Errors Decrease as E-Filing Increases

Tax practitioners and taxpayers made fewer errors on their tax returns this year.

The number of tax return mistakes is down 8 percent. The decrease may be due to a small increase in the number of returns that are filed electronically, known as e-filing, or by telephone. E-filing software automatically corrects math and tax computation errors. And e-filed returns with certain missing information are intercepted during transmission and corrected before the Franchise Tax Board's system accepts them.

Voice prompts and automatic calculations help cut down on errors on returns that are TeleFiled.

FTB found errors on 263,509 tax returns by the end of April. Most of the errors fall into these categories:

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FTB's Goldberg Honored



Franchise Tax Board Executive Officer Gerald H. Goldberg receives the American Society for Public Administration's "Outstanding Public Administrator" award from Joanne Kozberg, Secretary of the State and Consumer Services Agency. For more information, see page 8.

The April 15 Countdown

On April 15, the Franchise Tax Board's Taxpayer Services Center received a call from a man with a power of attorney for a missionary working on another continent. For several months, the man had been trying unsuccessfully to track down certain papers needed to fill out the missionary's tax return. He learned from FTB that the missionary did not have to file a return in California because her income was less than \$10,384.

Another caller said she wanted to pay a \$100 estimate toward her 1998 taxes because she does not like paying all at once. But she was a little short of cash. She learned that, because taxpayers are not required to make estimate payments of \$100 or less, she could send the money any time.

A man who recently retired called to report that he was making his best guess about his family income for 1998. But he was concerned about what would happen if he made a mistake and his guess was not close to the mark. He found out that FTB does not issue penalties to people in their first year of

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Tax News

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Tax Return Errors Decrease as E-Filing Increases

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Exemptions. Faulty exemption entries accounted for about 30 percent of all errors. In most cases, taxpayers transferred the total exemption amount to the wrong line.

Estimate amounts. In 14 percent of all errors, the amount of estimate payments listed on the tax forms as paid did not match the amount posted on FTB's system. And because FTB credits any unapplied miscellaneous payments as estimates, some of these "errors" result in refunds to taxpayers.

Tax computation. Almost 12 percent of the errors occurred because the tax was computed incorrectly.

Withholding. Withholding amounts were involved in 9 percent of all errors on 1997 tax returns. Most of the mistakes were made because amounts on two or more W-2 forms were incorrectly added. On some returns, however, the withholding amounts did not match amounts that employers reported to the Employment Development Department. Or the withholding was claimed by another state. In some cases, no W-2 forms were attached to the returns.

Deductions. Deductions accounted for 5.2 percent of all errors. Mostly, the standard deduction amount was incorrectly entered, but in some cases taxpayers listed itemized deductions that were less than the standard deduction.

State disability insurance. Another 5.2 percent of the errors involved state disability insurance amounts that did not match amounts on W-2 forms.

Nonresident. Almost 5 percent of the errors occurred because taxpayers filing nonresident returns incorrectly prorated their net tax liabilities.

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Tax Return Errors by Type

	% of total	Increase/decrease from previous year
Exemptions	30.1%	-12.9%
Estimate amounts	13.7%	-3.1%
Tax computation	11.9%	-14.7%
Withholding	9%	-1.6%
Deductions	5.2%	+2.5%
State disability insurance	5.2%	+18.8%
Nonresident	4.9%	-5.1%
Adjusted gross income	1.8%	-0.9%
Filing status	0.4%	-68.1%
Credits	0.1%	-9.2%
Miscellaneous	17.7%	16.6%
	100%	

Tax Return Error Rate

	Approximate % of all returns with errors
Form 540	33%
Form 540A	26%
Scanned returns	16%
540EZ	14%
540NR	8%
Electronically filed returns	3%
TeleFiled returns	Less than 1%
	100%

Electronic Funds Transfers Misdirected

Are your clients' electronic funds transfer (EFT) payments going to the right tax agency?

Since the beginning of the year, the Franchise Tax Board has received EFT payments intended for the Employment Development Department and the State Board of Equalization. EDD and SBE also have received funds intended for other agencies.

The misdirected payments began when Union Bank replaced Bank of America in January 1998 as the EFT bank for FTB, EDD and SBE. Each agency notified its EFT taxpayers in advance of its new bank and new bank account number. Apparently, however, some taxpayers did

not notice that each agency had a different bank account number; they used the same number for all three agencies.

When an EFT payment is sent to the wrong agency through either the Automated Clearing House (ACH) Credit or Fedwire payment method, it is not immediately credited to the taxpayer's account. As a result, the taxpayer receives a bill for the missing payment.

So, if any of your clients make EFT payments to FTB for bank and corporation taxes, EDD for disability insurance and personal income tax withholdings or SBE for sales or use taxes, make sure that the payment is sent to the correct bank account number for the agency. To check on the correct bank account number for FTB, see FTB Publication 3825, "Electronic Funds Transfer Program ACH Credit Information (1998 Edition)." Or call FTB's EFT Help Desk at the number listed in the box on this page. The box also lists EFT Help Desk numbers for EDD and SBE. The Help Desks also will provide general information on EFT and on becoming a voluntary EFT participant.

Information about FTB's EFT program is also on the Internet at the agency's <http://www.ftb.ca.gov/elecserv/efc.asp> address. □

Tax Return Errors Decrease

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Adjusted gross income. Less than 2 percent of the errors concerned California adjusted gross income. Either the amount was miscalculated or incorrectly copied from an accompanying schedule.

Miscellaneous. Other errors involved incorrect filing status, wrong refund amounts and various incorrect calculations.

Although exemption errors were made most frequently, the number is down from last year. So are errors in other categories such as tax computations, withholding and filing status. On the other hand, state disability insurance errors increased by almost 19 percent. (See chart on page 2.)

Almost 87,400 of the errors were detected on Form 540 returns that were manually processed. Another 68,400-plus errors occurred on manually processed Form 540A returns. More than 41,000 errors were found on image-processed, scannable Forms 540 and 540A returns. More than 36,000 occurred on manually processed Form 540EZ returns, and more than 21,000 were on manually processed Form 540NR returns. Only about 8,800 errors were made on electronically filed Forms 540, 540A, 540EZ and 540NR returns, and 574 were on TeleFiled returns. □

Some Tax Bills May Be Paid with Credit Cards

Taxpayers soon may use credit cards to pay some personal income tax bills from the Franchise Tax Board.

This summer, FTB will launch a pilot program with Paymentech that will allow certain taxpayers to use their MasterCard or VISA card to pay tax bills. Paymentech is the country's third largest processor of bank card transactions.

Taxpayers who may participate in the pilot program will receive an insert explaining how to make a credit card payment with the bills that FTB mails them.

Watch for more information about the credit card program in the September issue of Tax News. □

Electronic Funds Transfer Information

To obtain the proper bank account number for electronic funds transfer (EFT) payments to the Franchise Tax Board, the Employment Development Department and the State Board of Equalization or for other EFT information, call the:

EFT Help Desks

Franchise Tax Board
(916) 845-4025

Employment Development Department
(916) 654-9130

State Board of Equalization
(916) 327-4229

Order Tax Talk Video Course

The third volume in the Tax Talk learn-at-home video series is now available.

The "California Employment Factors" course includes a one-hour videotape, textbook, workbook and brief, "open book" examination for three credits.

The other courses in the series are "Office-In-Home Deductions" and "California Tax Rules for Nonresidents."

Each course costs \$60.

To order any of the courses, call (916) 845-7070 or visit the Franchise Tax Board's <http://www.ftb.ca.gov/education/taxtalk.htm> Internet address. □

Where to Find Free Small Business Seminar

Would you or your clients like to attend a free seminar for new or prospective small businesses?

The Service Corps of Retired Executives (SCORE) and the Small Business Development Center (SBDC) hold occasional seminars featuring the prize-winning "Striking Gold in California" video (see the March 1998 issue of Tax News).

The video is part of a tax education package for small businesses that includes a 40-page booklet and a directory of services and information sources. It was produced by the Small Business Tax

Connection, which is a committee of Franchise Tax Board, Internal Revenue Service, Employment Development Department and State Board of Equalization representatives.

For information on seminars in your area or for a copy of the booklet, which covers state and federal income and employment tax and state sales tax information, contact a local chapter of SCORE or the SBDC. You also may contact the State Board of Equalization at its <http://www.boe.ca.gov/sbtcon.htm> Internet address for a copy of the booklet. □

The April 15 Countdown

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retirement because estimating income is difficult the first time out.

All three callers hung up happy. Like many April 15 callers, they got good news. For others, it came in the form of an application that would allow them to pay their tax liabilities in installments. Others could not find the tax forms they needed on the last day for filing. Some were directed to FTB's Internet address where they could download and print tax forms. Those without Internet access were told where they might find forms locally.

Some callers who had filed earlier wondered why their refunds had not materialized. In these cases, refunds had been applied to unpaid tax liabilities from previous years or to debts owed to other agencies, and the taxpayers had not yet received notification.

In all, the Taxpayer Services Center answered 24,171 calls from taxpayers on April 15. On the average, calls took 3.4 minutes. The average time that callers spent on hold was just under three minutes. And the average taxpayer mood, despite the rapidly approaching midnight tax deadline, was calm and considerate.

In addition to the calls coming in to the Taxpayer Services Center, FTB's interactive voice response telephone

system received another 67,101 calls on April 15. More than 27,000 of them were placed by people who wanted to file their tax returns by telephone. Another 17,702 accessed the system's recorded answers to "Frequently Asked Questions." And almost 11,300 people called on April 15 to find out when they would receive their refunds.

By April 15, tax professionals had already done their homework. FTB's Tax Practitioner Support Unit took only 537 calls that day. And the longest anyone waited to be connected was 98 seconds.

FTB's Internet Web site was a popular place on April 15. Close to 35,400 users visited the site that day and downloaded 150,354 tax forms. Although an analysis of forms downloaded on April 15 has not been completed, the personal income tax resident booklet accounted for 32 percent of all downloads from January 1 through March 31. Another 13 percent of the downloads were the personal income tax nonresident booklet. The 540EZ was downloaded by 6 percent of the site visitors, the 540 by 4 percent and the 540A and 540NR by 3 percent each. The remaining 39 percent of downloads were for various personal income tax schedules, bank and corporation forms and forms for previous years. □

Free Seminar Looks at “Taxing Perceptions”

In the fall, you can do more than listen and learn at a free one-day seminar. You also can express your own ideas about issues that affect your tax practice, and you can gain six continuing professional education credits.

The Franchise Tax Board and the Internal Revenue Service will present the “Taxing Perceptions” seminar three times in each of two cities. In Oakland, the seminar will be held on September 23, 24 and 25. In Sacramento, it is scheduled for October 6, 7 and 8.

The seminar will put you face-to-face with FTB and IRS staff. In a three-hour morning session, you will be invited to participate in discussions on how practitioners and tax administrators “stereotype” each other, explore common misconceptions and expectations that each group has and discuss the tactics each group uses to accomplish its objectives. In the afternoon, after a no-

host lunch break, you may attend one of four three-hour sessions. The choices are a bankruptcy and lien seminar, an offer-in-compromise session, a penalty workshop/alternative documentation discussion and a seminar titled “Trusts – The Good, the Bad and the Ugly.”

The deadline for registration is September 4, 1998. If you are interested, sign up soon because seating will be limited to 75 participants on each day. To make a reservation, contact Bob Meyer at the Internal Revenue Service by mail at 4330 Watt Avenue, SA 2000, North Highlands, CA 95660 or by fax at (916) 974-5936.

When you register, you must make a first and second choice for both the seminar date and the afternoon program.

For more information, contact FTB at its <http://www.ftb.ca.gov> Internet address or call the Internal Revenue Service at (916) 974-5471. □

Why Taxpayers Fail to File

Why do taxpayers fail to file tax returns?

Each year, the Franchise Tax Board sends notices to about 600,000 individuals, informing them that they appear to have a filing requirement and that no tax return is on file. Many of these individuals are quick to tell FTB why they did not file. Some of them are right; they had no filing requirement. But some are mistaken.

Here are three of the most common misconceptions that nonfilers have about paying taxes. Nonfilers often tell FTB:

“Sure, I sold my personal residence during the tax year in question. But I rolled the gain over into a new home. So, I don’t need to file a tax return.”

The response is “Yes, you probably do.” When an individual’s gain on the sale of a home, combined with other income from California sources, is above the minimum income threshold, the individual needs to file a tax return to report the gain even though it is rolled over. This will also be true for individuals who take advantage of the new law that allows an exclusion of a home sale gain up to \$250,000 or \$500,000, depending on marital status.

The individual must file a tax return with the appropriate schedules, even if no tax is due.

“I had my own business. But even though I had a lot of gross receipts, I ended up with a loss. So, I don’t need to file a tax return.”

This case is similar to the above. If the amount of gross receipts for the business, combined with all other income from California sources, is above the minimum threshold, the business owner must file an income tax return with appropriate schedules attached.

“Yes, I am a partner in a California-based partnership. But I don’t live in California. So I don’t need to file a California income tax return.”

Individuals who have income from California sources are taxed on that income, no matter where they live. So, a nonresident with income from California, except for California-sourced pension income, needs to file a tax return with California. □

FTB Calendar

July

- 50,000 demand to file notices are mailed to individuals who failed to file 1996 tax returns.
- 40,000 Notices of Proposed Assessment are mailed to individuals who did not respond to demand to file notices issued in May for 1996 tax returns.
- Notices of Proposed Assessment for corporations’ failure to file 1995 tax returns begin finalizing. Those corporations will receive Notices of Balance Due.
- 20 Previous month nonresident withholding payments are due if total withholding exceeded \$2,500.

August

- 25,000 demand to file notices are mailed to individuals who failed to file 1996 tax returns.
- 30,000 Notices of Proposed Assessment are mailed to nonfilers of 1996 personal income tax returns.
- Notices of Proposed Assessment for corporations’ failure to file 1995 tax returns begin finalizing. Those corporations will receive Notices of Balance Due.
- 20 See July 20.
- 30 Last day to file Homeowner and Renter Assistance claims.

September

- 30,000 Notices of Proposed Assessment are mailed to individuals who did not respond to demand to file notices for the 1996 tax year.
- 40,000 demand/

Send Partnership Schedule K-1 on CD-ROM

The newest way for your clients to save paper when they file partnership Schedule K-1s is to file on a CD-ROM.

Starting now, the CD-ROM joins magnetic tape, tape cartridges and diskettes as electronic alternatives to filing the Schedule K-1 (565), "Partner's Share of Income, Deductions, Credits, etc." on paper.

For more information, visit the Franchise Tax Board's <http://www.ftb.ca.gov/electserv/bus.asp> Internet address. Or call the electronic filing Help Desk at (916) 845-0353 between 8 a.m. and 5 p.m. □

New Software for Editing Partnership Schedule K-1s

TestWare, a new, free software program for editing partnership Schedule K-1s on diskette, is now available from the Franchise Tax Board.

For the past three years, FTB has asked partnerships to voluntarily submit their Schedule K-1 (565), "Partner's Share of Income, Deductions, Credits, etc.," on magnetic media. The choices are magnetic tape, cartridge, diskette and now CD-ROM (see article on this page).

However, until now, partnerships could not obtain software that would allow

them to edit K-1 files before sending them to FTB. As a result, files that failed FTB's mainframe edit program were sent back to partnerships for correction. In some cases, several tries were necessary before the entire Schedule K-1 file could be accepted.

TestWare was designed as a tool in preparing magnetic media California Schedule K-1s (565) files. The software allows transmitters to test files before

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Fiscal-Year Filers: What Year Is It Anyway?

Are your fiscal year-end corporation clients filing their tax returns on forms for the correct year?

On the Form 100, "California Corporation Franchise or Income Tax Return," the income year shown in the upper left hand corner (see example below) should be the same year that your clients fill in for the "For income year beginning" space. The "ending" year space should be filled in with the date that is the end of the accounting period.

Taxpayer confusion about which form to use surfaced when the Franchise Tax Board recently sent demand to file notices and Notices of Proposed Assessment to corporations that failed to file a 1995 return. A number of fiscal year-end corporations responded by filing their 1995 tax returns on a form for the wrong year. FTB has notified these corporations that they filed using the wrong Form 100. The corporations still have time to file on the right form. □

Start of Fiscal Year Determines Form to File

INCOME YEAR			FORM					
1994			100					
California Corporation Franchise or Income Tax Return								
For income year beginning		MONTH July	DAY 01	YEAR 1994	and ending	MONTH June	DAY 30	YEAR 1995
Affix Preaddressed Label				E Was the corporation's income included in a consolidated federal return?		<input type="checkbox"/> Yes <input type="checkbox"/> No		
California corporation number		Federal employer identification number		F Does this corporation		<input type="checkbox"/> Yes <input type="checkbox"/> No		

Did your corporate clients file 1995 fiscal-year tax returns on the wrong form? The return for a fiscal year that begins in 1994 and ends in 1995 should be filed on the "Income Year 1994" Form 100, "California Corporation Franchise or Income Tax Return."

Finding Taxpayers on the Move

Each year, about 19 million people in the United States move to a different address. However, not all the Californians among them inform the Franchise Tax Board when they move.

The FTB program that notifies nonfilers of their requirement to file a tax return is working to improve the number of good addresses on file. In the past three years, FTB has been able to reduce by more than 80 percent the number of nonfiler tax notices that the post office is unable to deliver due to bad addresses.

Annually, FTB sends out more than 600,000 notices to people who appear to have a requirement to file a tax return but who fail to do so. Traditionally, about 80,000 of these notices are returned by

the post office as undeliverable, and FTB has been unable to locate the taxpayers' new address. However, in the past three years, FTB has reduced the number of undeliverable nonfiler notices to approximately 15,000.

To find current addresses for nonfilers, FTB checks with other tax agencies. If these efforts are unsuccessful, FTB attempts to get up-to-date addresses on taxpayers from their employers and credit bureau reporting services.

Although the 80-plus percent reduction in bad addresses is significant, FTB's nonfiler program is continuing to look for new ways of finding correct addresses for all taxpayers. □

New Software for Editing Partnership Schedule K-1s

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submitting them. As a result, the files should be error-free from the start.

TestWare provides data integrity edits only. It does not perform calculations. When files fail the edit, the errors are displayed so that changes can be made.

The software is available in both Windows 95 and Windows 3.X versions on the same disk. It is a personal computer (PC) based program and is designed for partnerships that submit their files on diskettes. Any partnership that currently sends Schedule K-1s to FTB on magnetic tape or cartridges can download the mainframe information to a PC for testing purposes.

You can obtain the TestWare software without charge by downloading it from FTB's <http://www.ftb.ca.gov/elecserve/bus.asp> Internet address. Or call the electronic filing Help Desk at (916) 845-0353 between 8 a.m. and 5 p.m. You also can obtain more information about filing Schedule K-1s from FTB Publication 1062, "Guide for K-1 (565) Filing By Diskette or Magnetic Media," which is available on the Internet and from the Help Desk. □

Head of Household Symposium? Stay Tuned

A Franchise Tax Board symposium on head of household issues is still on the drawing board, due to the interest that a significant number of tax professionals expressed.

FTB is analyzing responses to a survey published in the March Tax News. It asked interested tax practitioners if and when they would like the symposium to take place, what issues they would like covered and what other ways they would like to receive head of household filing status information.

Since the March survey, FTB sent questionnaires to a randomly selected group of 500 taxpayers to see if any would be interested in joining tax professionals for the symposium. Responses, requested by June 25, had not been tallied by press time.

The symposium is tentatively scheduled for sometime in January 1999, although the date is subject to change. □

FTB Calendar

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- questionnaire notices to file are mailed to corporations that failed to file 1996 returns.
- Notices of Proposed Assessment for corporations' failure to file 1995 tax returns begin finalizing. Those corporations will receive Notices of Balance Due.
- 4 Last day to register for FTB/IRS seminar, "Taxing Perceptions."
- 15 Personal income tax estimate payments are due.
- 20 See July 20.
- 23 FTB, IRS hold free "Taxing Perceptions" seminar in Oakland.
- 24 FTB, IRS repeat "Taxing Perceptions" seminar in Oakland.
- 25 FTB, IRS repeat "Taxing Perceptions" seminar in Oakland.

October

- 18,000 Notices of Proposed Assessment are mailed to individuals who did not respond to demand to file notices for the 1996 tax year.
- 6 FTB, IRS hold free "Taxing Perceptions" seminar in Sacramento.
- 7 FTB, IRS repeat "Taxing Perceptions" seminar in Sacramento.
- 8 FTB, IRS repeat "Taxing Perceptions" seminar in Sacramento.
- 15 Final extended due date for personal income tax returns.
- 20 See July 20.
- 26 Last day for postmarked California Tax Policy Conference registration, to avoid late fee. □

News from EDD

Tax News Available in Electronic Versions

Tax News is now available on the Internet and by E-mail, as well as in print.

For Internet viewing or for an E-mail subscription, contact Tax News at the Franchise Tax Board's <http://www.ftb.ca.gov> Web site. □

Seminars Offered

Every month, the Employment Development Department offers seminars to help employers comply with California employment tax laws.

Topics covered in the seminars include state payroll reporting requirements, preparing payroll tax returns, avoiding unnecessary tax liabilities, distinguishing between independent contractors and

employees, new laws, emerging issues and EDD services.

For a listing of seminars, contact EDD at its <http://www.edd.cahwnet.gov> Internet address. Click on "For Employers" and then "Attend a Tax Seminar." You also may call or visit your local Employment Tax Customer Service office. Or call (916) 464-3502. □

Goldberg Named Outstanding Public Administrator

Gerald H. Goldberg, the Franchise Tax Board's Executive Officer, was named "Outstanding Public Administrator" by the Sacramento Chapter of the American Society for Public Administration (ASPA).

ASPA is a national organization dedicated to advancing the science, processes, art and image of public administration. The award was presented at a ceremony on June 10.

Goldberg received the award from Joanne Kozberg, Secretary of the State and Consumer Services Agency, who nominated him for the honor. In her nomination letter, Kozberg called Goldberg "an advocate for continuous

improvement in government" and "a leader in the efficient and effective use of strategic and business planning technology and activity based costing." She also cited his "efforts to improve communications with taxpayers and simplify filing."

At the award ceremony, Kozberg praised Goldberg for, among other things, creating a notable "corporate and family culture" at FTB and what she termed "the best" technical procurement policies in the state. She also stated that FTB is the nation's model tax agency.

Goldberg has served as FTB's Executive Officer since 1980. □

Who Gets Direct Tax Refund Deposits?

About 184,300 California taxpayers took advantage of the Franchise Tax Board's offer to directly deposit their refunds in their bank accounts.

Only taxpayers who filed tax returns electronically qualified for direct deposits this year, although FTB is looking into extending the opportunity to TeleFile and paper filers in future years.

About 835,500 taxpayers filed their 1997 tax returns electronically. The 184,300

who opted for direct refund deposits represent almost 28 percent of the approximately 659,400 electronic filers who received refunds. The rest received paper refunds.

Approximately 121,400 electronic filers had a balance due. And close to 55,000 more electronic filers came out even on April 15. □

E-Filing: Slowly, Surely Making Gains

For most California taxpayers, filing a tax return means mailing a paper document.

Although paper tax returns still predominate, electronic methods of filing, known as e-filing, are expected to double by the year 2000.

Currently, 92 percent of all tax returns filed are on paper. About 60 percent of the paper returns are processed by manually entering the data on computers. The rest of the paper returns are "scanned" by image processing equipment, which is a faster, less expensive process. Six percent of this tax season's tax returns were electronically filed, and two percent were TeleFiled.

Along with the increase in e-filing this past season, the Franchise Tax Board experienced a few problems that have been ironed out. For example, FTB erroneously sent a Return Information Notice to about 60,000 e-filers. FTB subsequently sent out a letter of explanation and apology to the affected taxpayers and tax practitioners. □

Refunds and Credits, Deficiency Assessments: When Does Time Run Out?

Do your clients know how long they have to claim a refund when they overpay their taxes? Do they wonder how much time the Franchise Tax Board has to allow a refund or credit or to propose a deficiency assessment?

The laws that establish the statutes of limitations for claiming refunds or issuing credits and for assessing deficiencies set different expiration dates effective for taxable or income years beginning on or after January 1, 1992.

A taxpayer must claim a refund or FTB must allow a credit by the later of four years from the date that the return was due, without regard to extensions, or within one year after an overpayment was made. On the other hand, FTB may

FTB, IRS to Hold Free E-File Seminars

Everything you always wanted to know about electronic filing will be discussed at free e-file seminars in the fall.

The Franchise Tax Board and the Internal Revenue Service are co-sponsoring the seminars where you can learn about everything from how to fill out an e-file application to how to read the acknowledgment report you receive when your tax returns are accepted by an e-file system. The seminars will be held in September, October, November and December.

During the summer, tax practitioners will receive flyers with instructions on registering. You will be able to register either by fax or on-line at FTB's Internet site.

The flyers also will list seminar schedules by IRS district. Although the schedule for the Central California IRS District is not yet available, see the listing on this page for seminars in the Los Angeles, Southern California and Northern California IRS Districts. □

E-File Seminar Schedule

Franchise Tax Board and Internal Revenue Service e-file seminars are scheduled for the Los Angeles, Southern California and Northern California IRS Districts (see article on this page). Central District seminars will be announced later.

Los Angeles District

September 17 – Los Angeles
September 22 – Diamond Bar
September 29 – Cerritos
September 30 – Van Nuys
October 7 – Diamond Bar
October 8 – Lawndale
October 15 – Los Angeles
October 20 – Cerritos
October 28 – Van Nuys
October 29 – Lancaster
November 5 – Los Angeles
November 12 – Lawndale
November 19 – Van Nuys

Southern California District

September 25 – San Diego
September 29 – San Bernardino
October 1 – Costa Mesa
October 6 – Long Beach
October 8 – Palm Springs
October 14 – Laguna Niguel
October 22 – El Centro
October 27 – Oceanside
October 29 – Victorville

Northern California District

September 22 – Oakland
September 28 – Richmond
September 28 – Santa Rosa
September 29 – Eureka
September 30 – Willits
October 6 – San Francisco
October 16 – Redwood City
October 20 – Stockton
October 21 – Chico
October 22 – Walnut Creek
October 27 – North Highlands
October 29 – Vallejo
November 5 – Corte Madera
November 18 – North Highlands
November 19 – Hayward
November 30 – Redding
December 4 – Oakland
December 10 – North Highlands
December 17 – North Highlands □

Manufacturers' Investment Credit: For Your Information

Information that will help your clients better understand the manufacturers' investment credit (see article on this page) is available from the Franchise Tax Board.

FTB Publication 1113, "Frequently Asked Questions About the Manufacturers' Investment Credit (MIC)," provides answers to 19 questions about the credit. The questions include "How is the MIC claimed?" and "Do leases qualify for the MIC?" For a copy, visit FTB at its <http://www.ftb.ca.gov> Internet address. Click on "Tax Forms" and scroll to "Miscellaneous California Income Tax Forms, Instructions and Publications." Or write Tax Forms Request, P.O. Box 307, Rancho Cordova, CA 95741-0307. Or you may call (800) 852-5711.

You also can obtain form FTB 3535, "Manufacturers' Investment Credit," from the same FTB sources. The form includes instructions that feature the Standard Industrial Classification (SIC) Manual's Division D listings.

Also, see MIC regulations at Title 18, California Code of Regulations, Sections 17053.49-0 through 11 and 23649.0 through 11.□

Manufacturers' Investment Credit: What "Qualified" Means

The following overview of the manufacturers' investment credit is the first of a series. Other articles will deal with errors that taxpayers frequently make in claiming the credit.

Qualified taxpayer, qualified cost and qualified property are the three key requirements for claiming the manufacturers' investment credit (MIC). Do your clients understand what "qualified" means in each case?

The MIC is a 6 percent credit for the qualified cost for qualified property placed in service in California. Although 1995 is the first year in which the credit can be claimed, the credit applies to costs actually paid on or after January 1, 1994.

Taxpayers who claim the MIC must meet all three key requirements:

Qualified taxpayer. The taxpayer can be an individual, a corporation, an S corporation, a partnership, a limited liability company taxed as a partnership, an estate or a trust. Determining whether taxpayers are "qualified" is the first step in establishing eligibility for the credit. In order to claim the MIC, taxpayers must own at least one operating establishment classified under Division D, Manufacturing, of the 1987 edition of the Standard Industrial Classification (SIC) Manual, SIC codes from 2011 to 3999. (See "Manufacturers' Investment Credit: For Your Information" on this page.)

For MIC purposes, ignore principal activity codes on the state and federal tax returns.

Qualified costs. For costs to qualify for the MIC, three requirements must be met:

- The costs must be paid or incurred for acquiring, constructing or reconstructing qualified property.
- The taxpayer must directly or indirectly pay California sales or use tax on all costs, except for qualified capitalized labor costs.
- The costs must be properly chargeable to the taxpayer's capital account (depreciated).

Capitalized labor costs for constructing or modifying qualified property can qualify for the MIC as long as they meet the definition of "direct" labor costs under the federal uniform capitalization (UNICAP) rules. (See FTB Legal Ruling 98-1, "Manufacturers' Investment Credit - Capitalized Costs of Labor for Engineering and Design," at FTB's <http://www.ftb.ca.gov> Internet address.

Qualified property. Qualified property must meet a four-prong test. It must be:

- Tangible personal property.
- Internal Revenue Code Section 1245(a) property.
- Property used in a manufacturing establishment listed in the SIC manual's Division D.
- Property used at least 50 percent of the time for manufacturing, refining, processing, fabricating, recycling, research and development or measuring, testing or repairing otherwise qualified property.

Tangible personal property means any tangible property except land and improvements. However, special purpose buildings and foundations are the exceptions to the rule. Both can qualify even though they are not IRC Section 1245(a) property. Generally, this exception applies to "clean rooms" used by certain qualified taxpayers in manufacturing computer and office equipment (SIC codes 3571-3579 inclusive) or electronic components and accessories (SIC codes 3671-3679 inclusive), commercial physical and biological research (SIC code 8731) or biopharmaceutical activity (SIC codes 2830-2836 inclusive). However, special purpose buildings and foundations do *not* include:

- Buildings designed and constructed or reconstructed principally as general-purpose manufacturing, industrial or commercial buildings.
- Research facilities that are used primarily before and/or after the manufacturing process.

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Withholding Required on Payments to Nonresidents

Recently, the Franchise Tax Board sent letters to a number of business entities that apparently failed to withhold 1996 taxes on amounts paid to nonresident independent contractors.

Your California clients who make payments to nonresidents are required to withhold taxes under certain circumstances and forward the withholdings to FTB. The withholding rate is 7 percent of the gross payments of California source income made to nonresidents. The withholding requirements were established to promote voluntary compliance with California tax laws among nonresident individuals and entities that may be unaware of their filing requirements.

Your clients that do not withhold taxes on payments to nonresidents may be liable to pay the lesser of the amount of taxes due from the nonresident or the amount that should have been withheld. A failure to withhold also can result in penalties and interest. However, FTB's policy is to educate business entities about withholding requirements and help them establish withholding procedures.

Generally, corporations, other business entities and government bodies must withhold taxes on payments to nonresidents if the payments are more than \$1,500 for the year and are one of the following:

- For services performed in California by a nonresident independent contractor. (Nonresident independent contractors are not employees. Withholding on wages paid to employees is collected by the Employment Development Department, not FTB.)
- For *commercial* rents or lease payments for property located in California.
- For royalty payments for natural resources located in California.
- Distributions from California estates or California trusts.

Withholding is not required for certain payments to nonresidents. These may include, but are not limited to, payments:

- For goods.
- For income from intangible property such as interest or dividends.
- Made to a nonresident corporate director for performing director services, including attending a board of directors' meeting.
- Made to a payee for whom FTB has issued a written waiver of the withholding. In most cases, a waiver is authorized because the nonresident payee has a history of filing tax returns in California or shows, by making estimate payments, that it intends to file.

For more information on nonresident withholding, read FTB Publication 1023, "1995 Nonresident Withholding – Independent Contractor Rent and Royalty Guidelines." To obtain the publication, contact FTB at <http://www.ftb.ca.gov> on the Internet. Click on "Tax Forms" and then on "Miscellaneous Tax Forms." You also can obtain the publication by mail by writing to Tax Forms Request, Franchise Tax Board, P.O. Box 307, Rancho Cordova, CA 95741-0307.

If you have questions after reading Publication 1023, call FTB's Nonresident Withholding staff at (916) 845-4900. And watch for more information on nonresident withholding in future issues of Tax News. □

Manufacturers' Investment Credit

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- Storage facilities that are used primarily before and/or after the manufacturing process is completed.

The MIC for special purpose buildings and foundations includes capitalized labor costs that are directly allocable to constructing and modifying the buildings and foundations. □

SBE Opinions

Appeals of Douglas and Barbara Broyles, et al., May 1, 1998. The State Board of Equalization overruled its previous decision in Appeals of Thomas J. and Gerd Perkins, et al., 96-SBE 010, April 11, 1996, Petition for Rehearing denied November 13, 1996, with respect to limited partners who "had no control over the decision as to whether to distribute the stock to partners, or to sell it in the partnership."

The SBE concluded that, as long as the taxpayer limited partner was a partner at the time the partnership purchased the subsequently sold "small business stock," the taxpayer's stock acquisition date is the date that the partnership purchased the stock. The partnership's purchase of the stock at issue in these appeals was in 1982, "after the effective date of the small business stock legislation." And the SBE stated that it was "confident that the Legislature's purposes in enacting SB 690 (the small business stock statutes) included providing incentives for such venture capital activity."

At press time, a case number had not been assigned to this opinion. □

Taxpayers “March” to File

In spite of media focus on taxpayers rushing to post offices late at night on April 15, most people file their California tax returns earlier.

The most popular month for filing tax returns is March.

More than 2.5 million California taxpayers sent their returns to the Franchise Tax Board by mail, modem or telephone during March. □

Sign Up Now for November Tax Policy Conference

Tax experts from around the country will gather at the 1998 California Tax Policy Conference to debate the hottest issues facing tax professionals today.

The conference will be held at the Palace Hotel in San Francisco on November 11 – 13. Sponsors are the California Franchise Tax Board; the Institute of Governmental Affairs, University of California, Davis; and the California Policy Seminar, a University of California program.

Speakers include tax authorities from the practitioner, legal and university communities from California to Washington, D.C. and beyond.

Workshop topics include electronic commerce, allocating expenses, legislation, the IRS, court developments, litigation, state taxation of foreign income, burden of proof issues, Board of

Equalization issues, tax incentives and audit issues. The program has been approved for 13.5 continuing education credits by the State Bar of California and has been submitted to the National Registry of CPE Sponsors for approval of 13.5 hours of credits.

The conference fee is \$595 per person when it is paid with a registration postmarked October 26 or earlier. The fee covers workshops, general sessions, comprehensive conference material and a number of meals including a November 12 reception, dinner and entertainment. It does not include hotel accommodations.

To register or for more information, contact the FTB <http://www.ftb.ca.gov/education/ctpc> Internet site, fax (916) 845-5047 or call (916) 845-7998. □