



Tax News

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Deductibility of costs for energy saving projects where payments are made through property tax bills

We have become aware of taxpayer concerns regarding whether energy-saving projects paid through one's property tax bill qualify as deductible real estate taxes. These energy-saving projects include solar panels, air conditioning, roofing, windows, lighting controls, and landscape-related products. Often these projects are financed through the property assessed clean energy (PACE) program.

California conforms to federal law regarding real estate tax deductions. On May 25, 2016, the Internal Revenue Service issued "[Topic 503 - Deductible Taxes](#)" which provides specific guidance on this issue, including the following:

There are popular loan programs that finance energy saving improvements through government-approved programs. You sign up for a home energy system loan and use the proceeds to make energy improvements to your home. In some programs, the loan is secured by a lien on your home and appears as a special assessment on your real estate property tax bill over the period of the loan. The payments on these loans may appear to be deductible real estate taxes; however, they are not deductible real estate taxes. Assessments associated with a specific improvement benefitting one home are not deductible. However, the interest portion of your payment may be deductible as home mortgage interest. Refer to Publication 936, Home Mortgage Interest Deduction, to see whether you might qualify for a home mortgage interest expense deduction.

Therefore, under the above federal guidance, which appears consistent with federal guidance issued in 2013 (see Chief Counsel Advice 201310029), **neither** the principal nor interest amounts paid on a taxpayer's property tax bill for energy saving projects are deductible real estate taxes. However, taxpayers may be able to deduct some or all of the interest as a home mortgage interest deduction.

No cash policy exemption

On September 1, 2015, we fully implemented a "No Cash Policy" in all field offices. We implemented this policy to streamline processes, save costs, and reduce risk to our employees and customers. Although this policy achieved the intended goals, we are sensitive to the fact that our policy could create a hardship for taxpayers who are unable to open bank accounts. In order to address this concern, we established an exemption policy that will be implemented on July 1, 2016.

As of July 1, 2016:

- A taxpayer who needs to pay in cash must request an exemption to the “No Cash Policy” using the *No Cash Policy Exemption Request* form.
- To request an exemption, the taxpayer will need to provide an explanation for their inability to pay using our provided methods. The *No Cash Policy Exemption Request* form must be signed by the taxpayer, partner, corporate officer or POA.
- We will review the exemption request and mail a letter of determination to the taxpayer within two business days.
- If the exemption is approved, the taxpayer is responsible for contacting one of our six FTB field offices to make an appointment prior to making their cash payment.
- An approved exemption is good for all future transactions at any of our six offices.

Free FTB Form 587 webinar for withholding agents, payees, and tax practitioners

During this 10-minute webinar designed for withholding agents, payees, and tax practitioners, we cover the following key topics on FTB Form 587, Nonresident Withholding Allocation Worksheet:

- Form 587’s purpose.
- When withholding is required.
- Why withholding is required.
- When to complete Form 587.
- How to complete Form 587.
- Resources and contact information.

Register anytime to view our pre-recorded webinar.

For online information about California’s nonwage withholding program, go to ftb.ca.gov and search for **nonwage**.

Legislative bill watch list

As the legislative season comes to an end, many interesting tax bills have come to our attention. Many bills made the first cut, and with revisions moved to the second house. Many other bills did not make it out of their house of origin, and will not move on.

Here are a few interesting tax bills that remain alive:

- AB 567 – *Medical Cannabis Tax Amnesty Program*
- AB 1437 (Gray) – *Internet Fantasy Sports Game Consumer Protection Act*
- AB 1775 (Oberholte) – *Entity Tax Return Due Dates*
- SB 907 (Galgiani) – *Mortgage Forgiveness Debt Relief*
- AB 2318 (Low) – *Modify Definitions and Transfer Responsibility from FTB to FPPC Relating to Campaign Activity of Nonprofits Receiving Public Resources*

For more information on these and other bills we are currently analyzing, go to ftb.ca.gov and search **legislative information**. You can also follow bills as they are amended and move through the houses by using our Bill Tracking Report. You can also follow legislative bills by using [Legislative Counsel's website](#).

What should your client do if they can't pay their balance?

If your client is unable to pay their full balance due, they may be eligible to pay their balance by making installment payments over time.

Generally, your client is eligible to request an installment agreement (IA) through FTB's automated system if your client meets all of the following conditions:

- Their tax liability cannot exceed \$25,000.
- The installment period for your client's payments cannot exceed 60 months (5 years).
- Your client must have filed all required valid personal income tax returns.
- Your client does not have an existing installment agreement.

If your client is eligible, we recommend they make the largest monthly payment possible because their tax liability will continue to accrue interest and possibly penalties until it is fully paid.

If your client does not meet these criteria, or if your client currently has an order to withhold, continuous order to withhold, or earnings withholding order for taxes in effect, please call us to discuss options to resolve your client's account. We approve or reject installment agreement requests based on your client's ability to pay and their compliance history. We may file a lien and/or request a financial statement as a condition for approval.

What your client should know if approved for an installment agreement

By entering into an installment agreement, your client agrees to make timely monthly payments to pay the balance due. Your client also agrees to meet all future tax obligations, including filing valid tax returns timely and paying all future tax liabilities timely. Ensure that your client has enough withholding or estimated tax payments to pay their tax liability in full for future years.

By requesting an installment agreement your client should be aware of the following:

- If the installment agreement is through an authorized electronic funds transfer, payments will be automatically deducted from their bank account. Therefore, they must keep adequate funds in their bank account to satisfy monthly payments.
- Additional interest and some penalties continue to accrue while they make their scheduled payments.
- Your client agrees to pay a \$34 installment agreement fee. We add the fee to the balance due.
- We keep any state tax refund your client is due or becomes due during the term of the installment agreement and deduct it from the total amount they owe. The refund amount will not replace their monthly payment.
- If your client fails to make timely payments or if they incur an outstanding past due amount in a future year, your client will be in default of the installment agreement. If this occurs, we will send a notice of its intent to terminate the installment agreement.

3 ways to request an installment agreement

- Online
- Phone - Call 800.689.4776 to use the Interactive Voice Response (IVR) system 24 hours a day, 7 days a week.
- Mail - Complete and mail FTB 3567, Installment Agreement Request. Incomplete information will delay the processing of your request.

Good news, a chance to assign additional motion picture credit and more...

Here is your opportunity to increase your credit assignments! In the last edition, we brought you information about the new California Motion Picture and Television Production Credit and how to claim the old and the new credits. This time we bring you some exciting news about assignments!

We recently revised form FTB 3541, California Motion Picture and Television Production Credit, for all years with an open statute (i.e. 2012 to 2015). Now you will be able to include prior year assignable credit carryovers to determine the total amount of credit available for assignment in the current year. It is as simple as 1, 2, 3!

Step 1. Include **prior year** "assignable" credit to compute the total amount of credit available for assignment in the year being reported. (Credits that are purchased or received via assignment are not assignable.)

Step 2. If the total amount of credit available for assignment is greater than the amount assigned on the original return, then file an amended return.

Step 3. Complete form FTB 3541. List **both**, the originally reported credit assignments **and** the additional assignments. Attach the completed FTB 3541 to the amended return.

And more good news...

Motion picture credit that is in excess of current year tax liability is available for assignment.

What if you have both the old and the new credit? How will you determine the credit available for assignment? Depending on the amount of "assignable" credit available to you and the current year tax liability, you may need to apply the old or new credits, or both, to the tax liability in order to determine the credit available for assignment. For example:

Situation 1

Facts: Taxpayer has \$300,000 of old credit. They have \$200,000 of new credit. Current year tax liability is \$100,000.

Solution 1

	Old credit	New credit
Amount of credit available	\$300,000	\$200,000
Amount of tax liability reduced by credit	\$100,000	0
Credit available for assignment	\$200,000	\$200,000

Solution 2

	Old credit	New credit
Amount of credit available	\$300,000	\$200,000
Amount of tax liability reduced by credit	0	\$100,000
Credit available for assignment	\$300,000	\$100,000

Situation 2

Facts: Taxpayer has \$100,000 of old credit. They have \$200,000 of new credit. Current year tax liability is \$150,000.

Solution 1

	Old credit	New credit
Amount of credit available	\$100,000	\$200,000
Amount of tax liability reduced by credit	\$100,000	\$ 50,000
Credit available for assignment	0	\$150,000

Solution 2

	Old credit	New credit
Amount of credit available	\$300,000	\$200,000
Amount of tax liability reduced by credit	\$100,000	0
Credit available for assignment	\$200,000	\$200,000

Remember, if you're claiming the old credit and the new credit in the same year, you must complete a separate form FTB 3541 for each credit.

For additional information about the credit, please visit our motion picture and television production credit page.

Featured publication: Striking Gold in California

The California tax agencies (BOE, EDD, and FTB) and the IRS revised the [*Striking Gold in California, What You Need to Know about Taxes and Your Small Business*](#) publication. This is a great publication that you can share with clients and/or potential clients who are thinking about or starting a small business.

As you know, every year in California, thousands of new small businesses start up. Unfortunately, thousands also go out of business each year. Understanding their tax obligations can help small business owners be successful, so the Striking Gold in California publication describes each tax agency's role and provides appropriate resources within each agency, and gives easy-to-use information on income, sales and use, and employment taxes in an easy-to-read format.

In addition, the Index of Topics section identifies many free publications produced by the tax agencies that may be helpful to small business owners. Most forms and publications are available online or by telephone.

Ask the Advocate



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twitter.com/FTBAdvocate

Did your client receive a withholding adjustment this year?

Many practitioners have seen an increase in the number of withholding adjustments this filing season when compared to prior years.

Every filing season, FTB processes more than 15 million taxpayer returns and relies upon a variety of information sources to verify refund amounts before they are issued. FTB performs this verification to make sure the amounts listed on the return were correctly entered, to catch unintentional errors, and make sure the proper amount of withholding was applied to the return. When an error or discrepancy is identified, FTB issues a notice to explain that the refund or tax liability was adjusted above or below the expected amount. As a result, some taxpayers received smaller than expected refunds, some expecting a

refund instead received a balance due notice, while others who reported a balance due received an increase in the amount they owed.

FTB made several enhancements this year to rely more heavily on real-time information, and as a result, a larger-than-usual number of adjustments occurred due to problems related to wage withholdings. This generated an enormous wave of calls to FTB's customer service center from taxpayers and tax professionals with questions. FTB promptly issued apology letters to approximately 30,000 taxpayers whose returns should not have been adjusted, letting them know that any refunds would be mailed within 7 to 10 days. The first of these letters were sent with a mail date of June 15. Additionally, FTB increased the call center staff levels to provide immediate assistance to practitioners and taxpayers with questions and concerns.

The procedural changes FTB instituted were to not only catch reporting errors, but also prevent tax fraud and refund theft schemes, two trends which have increased dramatically worldwide. These changes, combined with late and some inaccurate reports from employers, caused some taxpayers to receive a reduced refund or an increase to their tax liability. FTB is currently reviewing the procedures used in the 2015 filing season to identify improvements which can reduce the number of adjustments in future years and provide quick feedback and resolution to taxpayers that need assistance.

Inside FTB

Dissolution/Cancellation process team

Here at FTB, we take our mission and values very seriously. Our mission is to provide the services and information to help taxpayers file accurate and timely tax returns and pay the proper amount owed. To accomplish this mission, we develop knowledgeable and engaged employees, administer and enforce the law with fairness and integrity, and responsibly manage the resources allocated to us. Because of this, when we receive consistent feedback from taxpayers about an issue, we try our best to help resolve it and provide taxpayer-centric solutions.

of the issues we regularly hear about from taxpayers, whether over the phone or at outreach events, is the confusion they have with the dissolution and cancellation process for business entities.

We put together a team with knowledge and expertise from different areas within FTB to provide end-to-end analysis of the current dissolution/cancellation process. We have been mandated to determine areas of improvement and to lay out a plan for possible changes. Possible areas of improvement could be through outreach and education programs, and/or process, administrative, or legislative changes.

In meeting our objectives, we also work with The California Secretary of State (SOS) and The Governor's Office of Business and Economic Development (GO-Biz), to discuss ideas to improve the current dissolution/cancellation process. We focused on three goals:

- Make the process easier for our business customers
- Hold intra-agency meetings
- Discuss how we can better communicate with each other

The current dissolution/cancellation process is a multi-step, multi-state agency process that is causing some confusion for taxpayers. With FTB, SOS, and GO-Biz working together on solutions, we hope to provide our taxpayers with an easier process to follow and complete.

Lastly, have your clients create a MyFTB account. Once registered, with just a few clicks, your clients can monitor their payments, check on the remaining balance due, and even request to skip a payment.

All About Business

What is a business trust?

In our May 2016 edition of Tax News, All About Business column, *What is a Disregarded Entity*, we explained that a business may organize under any number of legal forms, and that the decision on which legal form to use when organizing a business entity is important, as you may face different tax consequences. A separate existence of a business entity generally does not eliminate its requirement to pay taxes and the requirement to file a tax return. The May 2016 Tax News gave you examples of various entities commonly referred to as disregarded entities and what California law(s) requires. In this article, we look at business trusts.

When most hear or see the word “trust” most of us immediately think of arrangements created either by a will or by an inter vivos declaration¹ whereby a trustee or trustees take title to property for the purpose of protecting or conserving it for the beneficiaries. A trustee of such a trust would file a fiduciary income tax return. The trustee would file the federal Form 1041, *U.S. Income Tax Return for Estates and Trusts*. In California, the trustee files Form 541, *California Fiduciary Income Tax Return*.

A business trust is a little-known and little-used alternative for organizing a business in California.

The California Corporations Code includes business trusts in the definition of "other business entities."² The Corporations Code defines a business trust as a business organization formed as a trust.³ While the California Corporations Code governs the formation, operation, and control of an entity, California Revenue and Taxation Code (R&TC) provides the rules for taxation of these entities. R&TC Section 23038 provides that business trusts may be taxed under R&TC Section 23501 as a corporation or taxed as a partnership, but the classification of the entity as a partnership or corporation shall be the same as the classification for federal purposes.⁴ Regulation 23038(a) defines business trusts as devices created by the beneficiaries

¹ inter vivos is Latin for "among the living," usually referring to the transfer of property by agreement between living persons and not by a gift through a will.

² Corp. Code Sections 174.5 and 12242.5.

³ Corp. Code Section 12242.5.

⁴ R&TC Section 23038(b)(1)(B)(i).

to carry on a profit-making business which normally would have been carried on through business organizations that are classified as corporations or partnerships under the R&TC.

Business Trusts do not file on Form 541. These trusts file on either Form 565, *Partnership Return of Income*, or Form 100, *California Corporation Franchise or Income Tax Return*, depending on the character of the organization.

Remember when it comes to California, we follow the federal elections or classification of an entity; however, it is always important to check for California's specific requirements. Despite their existence as a "trust" under civil law, business trusts must be viewed differently for tax law purposes than they are for civil law purposes. Accordingly, tax questions involving business trusts and their beneficiaries must be addressed by using applicable tax law principles that flow from the entity choice the business trust makes for tax law purposes under the federal entity classification election system, and not from civil law principles. The federal entity classification election system (commonly referred to as the "check-the-box" regulations) state an arrangement will be treated as a "trust" if it can be shown that the purpose of the arrangement is to vest in trustee(s) responsibility for the protection and conservation of property for beneficiaries who cannot share in the discharge of this responsibility. Other arrangements that may be known as "trusts" are often called business or commercial trusts that were created as a way to carry on a profit-making business and are to either be classified as corporations or partnerships.

A business trust in California is taxed as a partnership (unless under the federal "check-the-box" regulations, it elected its classification for federal tax purposes to be classified as an association taxable as a corporation), meaning the trustees must give a K-1 to beneficiaries each year and then the beneficiaries pay income tax on the income.

Finally, there are special filing requirements for business trusts that are exempt organization trusts.

For more information about tax requirements and/or applying for tax exempt status, visit ftb.ca.gov and search for **exempt organizations**, or contact our Exempt Organizations Unit at **916.845.4171**.

Event Calendar

As part of education and outreach to our tax professional community, we participate in many different presentations and fairs. We now provide a calendar that shows the events we attend, as well as other events happening with us, such as interested party and board meetings.