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July 31, 1990

FTB Notice 90-4
410:BRL:CN-90-363

Re: Corporate Estimate Penalty Exceptions; State-Federal
Differences

As a general rule, corporations are required to prepay their tax in four installments, each amounting to 25% of the current year tax (Revenue and Taxation Code §25563). If this is not done, a penalty is imposed based on the "amount of underpayment," which is defined generally as the amount by which 90% of the required payment exceeds the amount actually paid.

AB 802 (Stats. 1989, Ch. 1352) substantially modified Revenue and Taxation Code §25954 and reduced the allowable exceptions to the estimated tax penalty, in partial conformity to federal changes. Specifically, the exception for tax on prior years' income using current year's rates was repealed, and the exception for payment of tax equal to the prior year's tax was modified for large corporations and large worldwide corporations to apply only to the first installment, with the provision that any reduction in the first estimate payment to meet the exception must be recaptured in the second installment.

~~Cumulative Computation~~

Unlike federal law, under California law the exceptions for all corporations are computed on a ~~cumulative~~ basis, as under §25954 a penalty is not imposed if the "~~total amount of all payments~~ of estimated tax paid on or before the last date required for payment" exceeds the prior year amount. Under federal law, the "required payment" is simply defined as 25% of the required annual payment. (Internal Revenue Code §6655(d)(1)(A).)

For example: A corporation (not a large corporation or large worldwide corporation) owed tax of \$100,000 in the prior year, and \$1,000,000 in the current year. For federal purposes, any installment payment of \$25,000 or more would satisfy the prior year's exception, and so no penalty would be imposed for that installment.

For California, if the corporation underpaid the second, third or fourth installment, the prior year exception would not apply unless the total amount of ~~all~~ installments paid amounted to 25% (\$25,000) for the first installment, 50% (\$50,000) for the second installment, 75% (\$75,000) for the third installment ~~and~~ 100% (\$100,000) for the fourth installment.

The consequence of failing an exception is that the estimate penalty is computed using ~~current year~~ amounts. In the example

NOTE: ((---)) = Indicates obsolete information.

above, a penalty would be imposed to the extent the first installment was less than \$225,000 (25% of 90% of \$1,000,000), the sum of the first and second installments was less than \$450,000, etc.

Large Corporation Restriction

Large corporations and large worldwide corporations are now allowed to base their first installment on the prior year's amount, but must recapture any reduction by increasing the second installment accordingly.

The corporation must meet both conditions of §25954(a)(1)(B) for the exception to apply: The first installment must be at least the prior year amount, and the second installment must include the recapture amount. If the first installment is less than the prior year amount or the second installment does not include the recapture amount (i.e., the sum of the two does not amount to 50% of the current year requirement), the exception is not met and a penalty is imposed on both installments based on the current year (25% of 90%) requirement.

DRAFTING INFORMATION

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