



02.27.2024

FTB NOTICE - 2024 – 01

SUBJECT:

Requests Involving Changes in Accounting Periods or Methods

PURPOSE:

The purpose of this notice is to provide guidance to taxpayers on the manner in which an election to change an accounting period or method is to be filed with the Franchise Tax Board ("FTB"). This notice includes and updates information previously provided in FTB Notice 2020-04. As such, this notice supersedes and replaces FTB Notice 2020-04.

BACKGROUND:

Sections 17024.5(f) and 23051.5(f) of the California Revenue and Taxation Code ("CRTC") provide that whenever a taxpayer is allowed or required to file an application or seek consent, the rules set forth in subdivision (e) of those sections shall apply to that application or consent.

CRTC sections 17024.5(e)(1) and 23051.5(e)(1) provide that a "proper election filed with the Internal Revenue Service in accordance with the Internal Revenue Code or regulations issued by [the Internal Revenue Service] shall be deemed to be a proper election for purposes of this part," unless otherwise provided in the CRTC or regulations issued by the FTB.

CRTC sections 17024.5(e)(3)(A) and 23051.5(e)(3)(A) state that to "obtain treatment other than that elected for federal purposes, a separate election shall be filed" with the FTB at the time and in the manner which may be required by the FTB.

Federal Form 1128, *Application to Adopt, Change, or Retain a Tax Year*, is used to request a change in the taxpayer's tax year. To request a change in a method of accounting, federal Form 3115, *Application for Change in Accounting Method*, is filed.

For combined reporting purposes, the members of a combined reporting group may elect to determine the total separate net income of each member of the group under accounting methods and other elections as authorized by Division 2, Part 11 of the CRTC. (Cal. Code Regs., tit. 18, section 25106.5-3(a).) If some or all the members of a combined reporting group elect to file a group return, then the key corporation acts as agent for the electing members. (Cal. Code Regs., tit. 18, section 25106.5(b)(14).) References in this notice to a

"taxpayer" includes each member of a combined reporting group that is eligible to determine the total separate net income of non-California members and to key corporations, where appropriate.

PROCEDURES:

I. Deemed California Consent:

If a taxpayer changes an accounting period or method for federal tax purposes, the change will apply for California purposes without any action by the taxpayer if California conforms to the underlying law being applied. This type of change is mandatory for California purposes unless the taxpayer makes a different California election to either (i) maintain its existing California accounting period or method, or (ii) change to a different accounting period or method than that elected for federal purposes. When deemed California consent applies, a request to either continue the use of the taxpayer's previous California accounting method or change to a different accounting method shall be treated as a different California election (see Section II below).

For changes involving deemed California consent, a copy of the approved federal election should be filed with the taxpayer's original California tax return for the taxable year in which the federal change is in effect. The taxpayer does not need to separately file federal Form 1128 or Form 3115 with the FTB.

The FTB will not issue an acknowledgment letter for deemed California consent changes.

Example 1

A taxpayer changes its federal accounting method and seeks the same change for California purposes. California conforms to the federal statute underlying the accounting method. Because California conforms to the underlying federal statute, there is deemed California consent. The taxpayer does not need to seek FTB consent but will need to provide a copy of the approved federal election with the taxpayer's original California tax return for the taxable year in which the federal change is in effect.

Example 2

A taxpayer changes its federal accounting method but seeks to retain the California accounting method used in the prior taxable year. California conforms to the federal law underlying both the previous federal accounting method and the newly adopted federal accounting method being applied. Because California conforms to the federal statute that provides for the newly adopted federal accounting method, there is deemed California consent and the newly adopted federal accounting method applies to California without any action by the taxpayer. In order to retain the California method used in the prior year, a different California election must be made by obtaining FTB consent.

A valid California election based on deemed consent remains valid to the extent California conforms to the underlying federal statute and allows the same method for California purposes. If federal law changes in a taxable year subsequent to when deemed California consent applied, and California does not conform to the federal change, the deemed California consent remains valid despite the change to the federal law that such deemed California consent was based on.

Deemed consent does not apply where California does not conform to the federal statute that provides for the new federal method. Therefore, if a taxpayer changes its federal accounting method but seeks to retain the California method used in the prior taxable year, the continued use of the previous California accounting method will not be considered a change of accounting method for California tax purposes if California does not conform to the underlying federal statute. The taxpayer does not need to seek FTB consent or file Form 3115 to maintain the accounting period or method used in the prior taxable year.

Example 3

A new federal law requires that a taxpayer change its federal accounting method from Method A to Method B but the taxpayer seeks to retain the Method A obtained in a prior taxable year under deemed California consent. California law allows both Method A and Method B. However, California does not conform to the change in federal law that requires taxpayers to change to Method B. Because California does not conform to the requirement to change accounting methods, the taxpayer's existing election on Method A remains valid and applies to California without any action by the taxpayer. The taxpayer does not need to seek FTB consent or file Form 3115 to retain the taxpayer's California accounting method.

II. Different California Election:

A taxpayer that (i) cannot rely on a federally approved request to change an accounting period or method for California tax purposes, (ii) desires to obtain California treatment other than that elected for federal purposes, or (iii) desires a change for California tax purposes only shall file a completed Form 1128 or Form 3115 with the FTB. The due date of the Form 1128 or Form 3115 is dependent on whether consent for the accounting period or method change would be considered automatic or non-automatic.

A. Automatic California Consent

With respect to a request to change an accounting period or method for California tax purposes only, the FTB shall grant automatic consent if the change would be eligible for automatic consent by the Internal Revenue Service and California conforms to the applicable Internal Revenue Code section that provides for the underlying accounting period or method being sought. If California does not conform to the applicable Internal Revenue Code section that provides for the accounting period or method being sought, there will not be automatic consent for California purposes.

For automatic California consent changes, a completed Form 1128 or Form 3115 should be filed with the taxpayer's original California tax return for the taxable year in which the change is in effect.

The FTB will not issue an acknowledgement letter for automatic California consent changes.

B. Non-Automatic Changes, FTB Consent Required

A request to change an accounting period or method for California tax purposes only that would not be eligible for automatic consent requires FTB consent. FTB consent is limited to the change of an accounting period or method and does not constitute FTB's approval of the taxpayer's use of the accounting period or method.

To obtain consent, a taxpayer should submit a request to the FTB by the due date required by law or at least sixty (60) days prior to the taxpayer's original return due date, including permissible extensions. This 60-day period would provide the FTB sufficient time to review the request and issue a determination letter. If consent is required and an original return is filed before receiving the consent of the FTB, the request will be denied.

A taxpayer's request for an accounting period or method change shall be considered denied if the FTB does not provide a written response within 60 days of receipt of said request.

Form 1128 and Form 3115 should be completed using appropriate California tax information. Do not use federal tax information, except that the Federal Employer Identification Number ("FEIN") should be used in the FEIN field. The California Corporation Number ("CCN") must be included on the top of the first page of the form.

Federal and California tax law differences should be accounted for when completing a Form 1128 or Form 3115. For example, line 24a of Form 3115 refers to a "User Fee." California does not charge a user fee for submitting the change request, and line 24a should be left blank.

Any references to the Internal Revenue Code on Form 1128 and Form 3115 or the form instructions should be read as referring to the Internal Revenue Code as applicable for California purposes, or the specific CRTC section, if any, that conforms to that federal provision.

Attach a cover letter to Form 1128 or Form 3115 submitted to the FTB with the name and CCN of the taxpayer, and a statement that the submission is an application for a "Change in Accounting Period" or a "Change in Accounting Method." Taxpayers should attach Form 3115 to their California return, as well as a California-specific pro forma Form 3115 showing adjustments to the impact of the accounting method change to reflect, for example, federal-to-state differences in depreciable basis, useful life, or applicable method of depreciation.

The appropriate federal form and cover letter should be sent to:

Franchise Tax Board
Change in Accounting Periods and Methods Coordinator
P. O. Box 1998
Rancho Cordova, CA 95812

Alternatively, the application may be faxed to (916) 855-5557.

CONTACT:

The principal author of this notice is Peter Kwok of the FTB's Legal Division. For further information regarding this notice, contact Mr. Kwok at the Franchise Tax Board, Legal Division, P.O. Box 1720, Rancho Cordova, California 95741-1720.