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Disaster loss deductions in California just got better

Legislature streamlines the process so taxpayers don't have to wait for authorizing legislation to throw back losses.

By Lynn Freer, EA
Publisher

Disaster victims often benefit from the ability to throw back any disaster loss under IRC §165(i) to the prior year and receive an immediate refund. Unfortunately, for years, taxpayers in disaster areas designated by the Governor, but not by the President, had to wait until the Legislature enacted legislation to be able to take advantage of those throwback provisions.

For tax years beginning on or after January 1, 2014, and before January 1, 2024, California law now provides immediate benefits for any loss attributable to a disaster for which only the Governor has declared a state of emergency. This means loss victims won't have to wait for California legislation to be enacted — often until October of the following year — to authorize the throwback election.¹

What the new law says

Taxpayers may now claim an IRC §165(i) throwback election on the California return for any disaster loss:

- Declared by the President (current law); or

- Declared by the Governor for any city, county, or city and county that is proclaimed by the Governor to be in a state of emergency.
In addition:
- A taxpayer may make the election on or before the extended due date of the tax return for the year of the loss. Federal law requires the election to be made on or before the original due date, not including extensions; and
- Unused disaster losses may create a net operating loss (NOL), which may be carried back two years from the year the disaster loss is recognized and carried forward for 20 years.

Four years of "instant" benefits

A big benefit to California's tax treatment is that for any loss declared by either the President or the Governor, a taxpayer may be able to obtain four years of immediate tax benefit: the current year, throwback to the immediate prior year for the disaster loss and, if an NOL is created or increased, an additional two years of carryback attributable to the NOL. Plus, remaining loss can also be carried forward.

EXAMPLE 10-1: Joe's crops in Humboldt County were destroyed in the 2015 fires for which the Governor declared a state of emergency. His vineyard was not insured, and his loss was \$300,000. Because the President did not declare the fires a disaster, he has no disaster loss for federal purposes. However, for California he has a disaster loss, and under IRC §165(i), he may claim the loss on either his 2015 or 2014 return.

Joe's income is approximately \$60,000 per year, and the unused loss will create an NOL.

If he elects to claim the loss on his 2014 return, he can carry back 75% of the unused loss to 2012 and 2013. If there is a loss remaining, he may carry the loss forward to the 2015 year. This provides him four years of refunds now.

If he does not make the throwback election, he will claim the loss on the 2015 return and may carry 100% of the NOL back to 2013 and 2014. But he won't be able to claim the disaster loss until he files the 2015 return in 2016.

In any event, he may carry any unused loss forward for 20 years from the year the loss is claimed.

See the chart below for the California disasters in 2014 and 2015 that qualify for the new loss treatment.

California Losses That Qualify for Disaster Loss Treatment

"State of emergency" declaration date	Type of disaster	Counties/cities impacted
May 14, 2014	Wildfires	San Diego
August 2, 2014	Wildfires	Amador, Butte, El Dorado, Humboldt, Lassen, Madera, Mariposa, Mendocino, Modoc, Shasta, Siskiyou counties

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August 24, 2104	Earthquake	Napa, Solano, and Sonoma counties (President previously declared a disaster area for parts of Napa and Solano counties)
September 17, 2014	Wildfires	El Dorado and Siskiyou counties
May 20, 2015	Oil spill	Santa Barbara county
July 31, 2015	Wildfires	Butte, El Dorado, Humboldt, Lake, Madera, Napa, Nevada, Sacramento, San Bernardino, San Diego, Shasta, Solano, Tulare, Tuolumne, and Yolo counties
September 2015	Wildfires	Amador, Calaveras, Lake, and Napa counties

Drought

On January 17, 2014, the Governor declared a state of emergency in California due to current drought conditions. As this disaster was not directed to a city or county, as required by R&TC §§17207.14 and 24347.14, the disaster loss throwback treatment is not available. In addition, a disaster loss, like a casualty loss, is one arising from fire, storm, shipwreck, or other casualty, or from theft.² The loss must be sudden in nature, and drought losses will usually not meet the requirements of casualty losses. See Rev. Rul. 77-490 for an example of a drought that did qualify.



¹ SB 35 (Ch. 15-230); R&TC §§17207.14, 24347.14

² IRC §165(h)(3)(B)

New conformity bills await Governor's signature

We will keep you posted as news develops.

By Renee Rodda, J.D.
Editor

As this issue of *Spidell's California Taxletter*® was going to press, several important bills were in limbo, waiting to see if the Governor will sign them. Here is a summary of those bills.

We will update you when the Governor takes action on each of these bills, and next month we will provide a detailed analysis of the ones he signs into law.

COD conformity

AB 99 (Perea) would extend California's partial conformity to principal residence COD relief for 2014 returns only. If the Governor signs this very late conformity, you can file those extended returns you have been holding on to.

We did send an e-mail to the Governor's office requesting he sign this bill immediately.

Conformity date

AB 154 (Ting) would update the IRC conformity date to January 1, 2015, for taxable years beginning on or after January 1, 2015.

Among other changes, the bill does the following:

- Increases the additional tax on nonqualified withdrawals from medical savings accounts (MSAs) from 10% to 12.5%;

- Retains the 7.5% threshold for medical expense deductions for California;
- Creates exceptions to the large corporate understatement penalty;
- Conforms to Foreign Account Tax Compliance Act (FATCA) information reporting for foreign financial assets, with modified penalty amounts;
- Excludes cell phones from listed property; and
- Conforms to IRC §6164, related to extension of time for payment of current year taxes by corporations expecting NOL carrybacks.

The bill does not conform to many common federal/state differences, including bonus depreciation, increased IRC §179, or real estate professional treatment.

ABLE accounts

AB 449 (Irwin) and SB 324 (Pavely) would conform to the federal ABLE Act under the Personal Income Tax Law and Corporate Tax Law, for taxable years beginning on or after January 1, 2016. The bills would establish an ABLE account program in California, and would require that the Board provide an annual listing of distributions to individuals that have an interest in an ABLE account to the FTB.

This conformity would mean that qualified distributions from ABLE accounts would not be taxable for California income tax purposes.

Roadmap to Understanding 2015 California Tax Legislation

We have created a document summarizing this year's most important tax legislation. The document contains a brief description of each bill, whether it has been discussed in *Spidell's California Taxletter*®, and a link to the California Legislative Information page for each bill.

Some of these bills have been signed by the Governor, and some are still awaiting his signature. We will continue to update the document as bills are signed.

To view the roadmap, go to:

[www.caltax.com/spidellweb/public/
editorial/2015CALegislation.pdf](http://www.caltax.com/spidellweb/public/editorial/2015CALegislation.pdf)



Wynne or lose: Fair apportionment remains the law

Supreme Court case involves credit for tax paid to other states.

By Cameron L. Hess, CPA, Esq.
Guest Contributor

The Supreme Court recently affirmed that the doctrine of fair apportionment under the Commerce Clause broadly applies to all taxpayers, individual and corporate, and all net income and gross receipts taxes. Practitioners should give careful review in California to its application to local business taxes.

The Wynne decision

In *Wynne*, two Maryland residents appealed their local state personal income tax assessments.¹ While the Maryland personal income tax on a Maryland resident's share of S corporation income earned out-of-state is allowed a state credit for tax paid to another state, Maryland law collects both (i) a state tax and (ii) a county tax (based on the Maryland

resident's county or an *in lieu* nonresident special rate for nonresidents). The county rate is a percentage of the state tax.

Maryland took the position that the county rate was not a state tax. Therefore, out-of-state tax paid on non-Maryland-sourced income taxed to Maryland residents was only credited against the Maryland "state rate" tax and not the county rate tax.

In reviewing this structure, the Supreme Court affirmed the Maryland high court decision that both the state and county taxes were in fact a state tax. Maryland's failure to credit out-of-state taxes paid against both the state rate and the county rate violated the dormant Commerce Clause in failing to provide a fair apportionment tax system.

The Court applied the doctrine of "internal consistency," finding that total taxes due would be higher for a Maryland resident who did business outside Maryland than one doing business wholly within Maryland, if another state imposed the same taxes and same rates as did Maryland.

Furthermore, while Maryland could have fixed the violation by several means, whether to expand the credit, tax only Maryland-sourced income (and drop the credit), or another apportionment system, Maryland failed to do that and therefore its tax was unconstitutional.

Dormant Commerce Clause

While the *Wynne* decision involves a unique income tax structure, wherein the state collects a "county rate," the Court recognized that fair apportionment must be given broad application. The Court undertook a lengthy discussion to clearly identify that it applied to taxes on gross receipts and income for both individuals and corporations. The Court further recognized that there are several different means for meeting the fair apportionment standard.

Application to California taxpayers

In California, for income tax purposes, fair apportionment of business income is generally based on apportioning business income within and without California, wherein the tax is only based on an allocation of net profits within California. While there were successful challenges a few years ago, based on California being a member of the Multistate Tax Commission, California's current system now requires a single-factor (market sales) approach. While there are special industry exceptions, the current option is not presently the subject of a major challenge.

On the other hand, city gross receipts taxes, particularly those with higher rates, other than major cities such as Los Angeles and San Francisco, have not been as well developed with respect to what is reasonable fair apportionment. Where a taxpayer is doing business within and outside a city, a practitioner should review the activities and the taxpayer's computation of taxes on gross receipts, and determine whether a system of fair apportionment has been allowed.

This review may result in significant tax savings, including obtaining an advisory letter from city council or an administrator as to what would be allowable as fair apportionment. If an agreement is not reached, careful documentation should be made as to what would be reasonable apportionment. In reviewing the method, a practitioner may apply the same internal consistency doctrine to determine if the apportionment is reasonable.

Lastly, where a dispute arises, a practitioner should advise a client that it is possible in dealing with fair apportionment issues to win the battle, but to not get a full recovery for the time and effort of the challenge.

Accordingly, it is in the best interests to try to resolve issues informally with respect to a city authority. First, documentation of a fair apportionment computation is critical, or it is possible

that no relief may be granted at an administrative or court level.² Second, pushing a matter to court, and a trial court's finding of an unconstitutional city gross receipts tax due to a failure of fair apportionment, does not guarantee full refund of business taxes paid. While appellate courts have differed, in *Ventas Finance II, LLC v. FTB*,³ after trial court judgment but before a hearing on the appeal, the California Court of Appeals allowed the FTB to offer the taxpayer "fair apportionment" of LLC fees after telling the taxpayer and the trial court that it lacked authority to do so. Accordingly, while ruled to be unconstitutional, the appeals court still allowed the FTB to fix the statute by offering a partial refund during the appeal.

About the author

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¹ *Controller of Treasury of Maryland v. Wynne* (May 18, 2015) U.S. Supreme Ct., Case No. 13-485

² *Appeal of Seventy Seven, LLC* (April 22, 2014) released August 2014 Cal. St. Bd. of Equal., Case No. 657975

³ *Ventas Finance II, LLC v. FTB* (2008) 165 Cal.App.4th 1207

Medical marijuana licensing, regulation awaits

But medical marijuana dispensaries/cultivators are still disallowed most tax deductions.

By Sandy Weiner, J.D.
California Editor

Almost 20 years after California voters passed Proposition 215, the Compassionate Use Act of 1996, authorizing the use of medical marijuana in California, the Legislature has finally passed legislation governing the medical marijuana industry. When this issue went to press, the Governor had not yet signed the bills. However, his office played a key role in negotiating their passage, so it is widely assumed he will sign them shortly.

With the exception of authorizing counties to tax medical marijuana businesses, there are no changes concerning the taxation of medical marijuana.

SB 420 (Ch. 03-875) allowed users to obtain a medical marijuana identification card from a physician and allowed patients and their primary caretakers "collectively and cooperatively" to cultivate marijuana for medical use without being subject to criminal sanctions. Beyond prohibiting these activities from being conducted in a "for profit" enterprise, and specifying how many plants each patient or primary caretaker could grow, state legislation did not provide much guidance as to who could "legally" (under state law, that is) grow, sell, and/or distribute marijuana.

On the last day of this year's legislative session, the General Assembly passed three bills, comprising the Medical Marijuana Regulation and Safety Act.¹

If signed by the Governor, the act will require all medical marijuana businesses, including cultivators, manufacturers, dispensaries, delivery services, etc., to obtain a state license(s), but only if they first receive a local permit, license, or other local authorization. Under the act, medical marijuana businesses will no longer be prohibited from making a profit.

Current dispensaries may continue to operate as they do today until at least January 1, 2018, when the formal state licensing process is expected to begin.²

This article provides a brief overview of the new legislation and summarizes the current California tax issues concerning medical marijuana businesses.

Local taxation

Although at one point it looked like the state would impose a new excise tax on medical marijuana, this provision was pulled out of the final bill versions that were passed. The only real reference to the taxation of medical marijuana is a new provision that authorizes counties, with approval by the voters, to impose a tax on medical marijuana businesses.³

Regulatory framework

The act puts primary control over the regulation and licensing of medical marijuana within a new Bureau of Medical Marijuana Regulation in the Department of Consumer Affairs, but spreads around regulatory and licensing responsibilities among a host of other agencies as well:⁴

- Bureau of Medical Marijuana: sole authority for licensure of transportation and storage, unrelated to manufacturing, of medical marijuana, including the establishment of appellation labeling standards similar to those used for the wine industry;
- Department of Food and Agriculture: oversees the cultivation and transportation of medical marijuana, including licensing of both indoor and outdoor cultivation sites and the development of a "certified organic designation program" for medical marijuana;
- State Department of Health: oversees the manufacturing and testing of medical marijuana, including developing standards for the production and labeling of all edibles; and
- Multiagency task force comprised of the Department of Fish and Wildlife and State Water Resources Control Board: addresses the environmental impacts of marijuana cultivation.

Licenses

Businesses will be required to secure a license and pay an annual license fee (the amount to be determined by the issuing agency). There are at least 12 different types of licenses, depending on whether the business is a cultivator (indoor, outdoor, mixed-light, small, medium, or nursery), manufacturer, tester, dispensary, distributor, or a transporter. Businesses will also be restricted to holding a license in only two separate categories.

Businesses operating without a license will be subject to penalties of up to twice the amount of the license fee for each day of noncompliance, and a court may order the destruction of all medical marijuana associated with the violation.⁵

Note: Individual patients and their primary caretakers may still grow medical marijuana without a license, up to specified amounts.

Physician restrictions

The act will only allow "attending physicians" (as defined in Health & Safety Code §11362.7) to prescribe medical marijuana and deems a physician to be engaging in "unprofessional conduct" if he or she prescribes marijuana without a physical examination or enters into any type of financial arrangement with a medical marijuana dispensary.⁶

Income taxation

Under IRC §280E, medical marijuana businesses are prohibited from claiming any deductions other than cost of goods sold (COGS).

California Personal Income Tax Law conforms to the IRC §280E prohibition, so individuals, sole proprietors, partnerships, and LLCs taxed as partnerships may only deduct COGS.

California's Corporation Tax Law does not conform to IRC §280E. This means that a corporate taxpayer (including an LLC taxed as a corporation) may be allowed full deductions for COGS and business expenses.

However, no deduction is allowed for COGS by either personal income or corporate taxpayers if the taxpayer was determined to be engaged in criminal profiteering or related activities enumerated in R&TC §§17282 and 24436.1. Those activities include drug trafficking. For this limitation to apply, a taxpayer must be found to be engaged in these activities through a final determination in a criminal proceeding, or a proceeding in which the state, county, city and county, city, or other political subdivision was a party. If such a determination is made, the taxpayer is prohibited from claiming all business expenses, including COGS.

For a discussion of the definition of a "determination," see "Medical marijuana can cause a tax headache" in the November 2012 issue of *Spidell's California Taxletter*®.

Medical expense deduction?

An amount paid to obtain a controlled substance (such as marijuana) for medical purposes is in violation of the federal Controlled Substances Act⁷ as the controlled substance isn't legally procured. As such, it is not a deductible medical expense, even if state law permits its use when prescribed by a physician and the taxpayer gets a prescription.⁸

California conforms to IRC §213,⁹ so no deduction is allowed for California purposes even though California allows the legal use when prescribed by a physician.

Sales and use taxes

All medical marijuana is subject to sales tax. Dispensaries are required to obtain a permit and pay taxes. Edibles are not considered food, but rather a food supplement, as most people are not consuming these for nutritional value. Delivery of marijuana is not exempt.

BOE offices are now accepting cash payments of sales taxes. However, many taxpayers have been subjected to penalties for failing to comply with EFT and e-filing requirements. According to BOE Chairman Horton, the BOE is granting waivers in this situation.

Cultivators may get resale exemption certificates from dispensaries.

Incentives

Medical marijuana businesses may qualify for the New Employment Credit, and cultivators may also qualify for the Research Credit, the partial sales and use tax manufacturer's exemption, and agricultural exemptions and credits.

Business licenses/fees

Localities either ban dispensaries or require dispensaries to obtain business licenses and pay local taxes/fees. Failure to comply with these requirements will transform a dispensary into an "illegal" activity.



¹ AB 243 (Wood), AB 266 (Bonta), SB 643 (Nazarian)

² B&PC §19320

³ B&PC §19348

⁴ B&PC §§19302.1, 19332

⁵ B&PC §19318

⁶ B&PC §2525.2

⁷ 21 USC §§801–971

⁸ Rev. Rul. 97-9; IRC §213

⁹ R&TC §17201

2015 California Tax Rates, Exemptions, and Credits

The rate of inflation in California, for the period from July 1, 2014, through June 30, 2015, was 1.3%. The 2015 personal income tax brackets are indexed by this amount.

Exemption credits

- Married/RDP filing joint, and surviving spouse..... \$218
- Single, married/RDP filing separate, and HOH \$109
- Dependent..... \$337
- Blind \$109
- Age 65 or older \$109

Phaseout of exemption credits

Higher-income taxpayers' exemption credits are reduced as follows:

	Reduce each credit by:	For each:	Federal AGI exceeds:
Single	\$6	\$2,500	\$178,706
Married/RDP filing separate	\$6	\$1,250	\$178,706
Head of household	\$6	\$2,500	\$268,063
Married filing joint	\$12	\$2,500	\$357,417
Surviving spouse	\$12	\$2,500	\$357,417

When applying the phaseout amount, apply the \$6/\$12 amount to each exemption credit, but do not reduce the credit below zero.

If a personal exemption credit is less than the phaseout amount, do not apply the excess against a dependent exemption credit.

Example of exemption credit phaseout

Joe is a single taxpayer with one dependent. His federal AGI is \$187,000. He must phase out each of his exemptions by \$24. That is, $(\$187,000 - \$178,706) \div \$2,500 = 4$ (always round up); $4 \times \$6 = \24 . His exemption credit for 2015 is \$398, calculated as follows:

Joe's personal exemption credit is..... \$109
 Less phaseout amount (\$ 24)
 Personal exemption credit allowed is \$ 85
 Joe's dependent credit exemption is \$337
 Less phaseout amount (\$ 24)
 Total dependent credit allowed is \$313
 Total exemption credits allowed is \$398

Reduction in itemized deductions

Itemized deductions must be reduced by the lesser of 6% of the excess of the taxpayer's federal AGI over the threshold amount or 80% of the amount of itemized deductions otherwise allowed for the taxable year.

- Single and married/RDP filing separate \$178,706
- Head of household..... \$268,063
- Married/RDP filing joint and surviving spouse \$357,417

Standard deductions

The standard deduction amounts for:

- Single and married/RDP filing separate \$4,044
- Married/RDP filing joint, head of household, and surviving spouse \$8,088
- Minimum standard deduction for dependents..... \$1,050

Miscellaneous credits

- Qualified Senior Head of Household Credit is 2% of California taxable income, with a maximum California AGI of \$69,902, and a maximum credit of \$1,317
- Joint Custody Head of Household Credit and Dependent Parent Credit are each 30% of net tax, with a maximum credit of..... \$431

Nonrefundable Renter's Credit

This nonrefundable, noncarryover credit for renters is available for:

- Single and married/RDP filing separate with a California AGI of \$38,259 or less..... \$60 credit
- Married/RDP filing joint, head of household, and surviving spouse with a California AGI of \$76,518 or less..... \$120 credit

Individual tax rates

- The maximum rate for individuals is 12.3%
- The AMT rate for individuals is..... 7%

The Mental Health Services Tax Rate is 1% for taxable income in excess of \$1,000,000.

AMT exemption

- Married/RDP filing joint, and surviving spouse.... \$87,627
- Single and head of household \$65,721
- Married/RDP filing separate, estates, and trusts \$43,812

AMT exemption phaseout

- Married/RDP filing joint, and surviving spouse..... \$328,601
- Single and head of household \$246,451
- Married/RDP filing separate, estates, and trusts ... \$164,299

FTB cost recovery fees

- Bank and corporation filing enforcement fee..... \$92
- Bank and corporation collection fee..... \$334
- Personal income tax filing enforcement fee..... \$79
- Personal income tax collection fee..... \$226

The personal income tax fees apply to individuals and partnerships, as well as limited liability companies that are classified as partnerships. The bank and corporation fees apply to banks and corporations, as well as limited liability companies that are classified as corporations. Interest does not accrue on these cost recovery fees.

Corporate tax rates

- Corporations other than banks and financials 8.84%
- Banks and financials..... 10.84%
- AMT rate 6.65%
- S corporation rate 1.5%
- S corporation bank and financial rate 3.5%

2015 California Tax Rate Schedules

Schedule 1 — Single or Married/RDP Filing Separate

If the taxable income is...

Over	But not over	Tax is...			Of amount over...
\$0	\$7,850	\$0.00	plus	1.00%	\$0
\$7,850	\$18,610	\$78.50	plus	2.00%	\$7,850
\$18,610	\$29,372	\$293.70	plus	4.00%	\$18,610
\$29,372	\$40,773	\$724.18	plus	6.00%	\$29,372
\$40,773	\$51,530	\$1,408.24	plus	8.00%	\$40,773
\$51,530	\$263,222	\$2,268.80	plus	9.30%	\$51,530
\$263,222	\$315,866	\$21,956.16	plus	10.30%	\$263,222
\$315,866	\$526,443	\$27,378.49	plus	11.30%	\$315,866
\$526,443	and over	\$51,173.69	plus	12.30%	\$526,443

Schedule 2 — Married Filing Joint or Qualifying Widow(er) with Dependent Child

If the taxable income is...

Over	But not over	Tax is...			Of amount over...
\$0	\$15,700	\$0.00	plus	1.00%	\$0
\$15,700	\$37,220	\$157.00	plus	2.00%	\$15,700
\$37,220	\$58,744	\$587.40	plus	4.00%	\$37,220
\$58,744	\$81,546	\$1,448.36	plus	6.00%	\$58,744
\$81,546	\$103,060	\$2,816.48	plus	8.00%	\$81,546
\$103,060	\$526,444	\$4,537.60	plus	9.30%	\$103,060
\$526,444	\$631,732	\$43,912.31	plus	10.30%	\$526,444
\$631,732	\$1,052,886	\$54,756.97	plus	11.30%	\$631,732
\$1,052,886	and over	\$102,347.37	plus	12.30%	\$1,052,886

Schedule 3 — Head of Household

If the taxable income is...

Over	But not over	Tax is...			Of amount over...
\$0	\$15,710	\$0.00	plus	1.00%	\$0
\$15,710	\$37,221	\$157.10	plus	2.00%	\$15,710
\$37,221	\$47,982	\$587.32	plus	4.00%	\$37,221
\$47,982	\$59,383	\$1,017.76	plus	6.00%	\$47,982
\$59,383	\$70,142	\$1,701.82	plus	8.00%	\$59,383
\$70,142	\$357,981	\$2,562.54	plus	9.30%	\$70,142
\$357,981	\$429,578	\$29,331.57	plus	10.30%	\$357,981
\$429,578	\$715,962	\$36,706.06	plus	11.30%	\$429,578
\$715,962	and over	\$69,067.45	plus	12.30%	\$715,962

Individual Filing Requirements

Filing Status	Age as of December 31, 2015*	California Gross Income			California Adjusted Gross Income		
		Dependents			Dependents		
		0	1	2 or more	0	1	2 or more
Single or head of household	Under 65 65 or older	16,256 21,706	27,489 30,131	35,914 36,871	13,005 18,455	24,238 26,880	32,663 33,620
Married filing joint, RDP, or separate	Under 65 (both spouses/RDPs) 65 or older (one spouse) 65 or older (both spouses/RDPs)	32,514 37,964 43,414	43,747 46,389 51,839	52,172 53,129 58,579	26,012 31,462 36,912	37,245 39,887 45,337	45,670 46,627 52,077
Surviving spouse	Under 65 65 or older		27,489 30,131	35,914 36,871		24,238 26,880	32,663 33,620
Dependent of another person — Any filing status	Under 65 65 or older	More than your standard deduction More than your standard deduction					

* If you turn 65 on January 1, 2016, you are considered to be age 65 at the end of 2015.

Ballot initiative filing fee increased

The change is in response to recent submissions of “outrageous” initiatives.

By Sandy Weiner, J.D., and
Kathryn Zdan, EA
Staff Writers

AB 1100 (Ch. 15-229) increases the filing fee from \$200 to \$2,000 to submit a proposed state ballot initiative to the Attorney General (AG) for preparation of a circulating title or summary.¹ The increased fee goes into effect on January 1, 2016.

Background

The \$200 fee was set in 1943 to cover the administrative costs by the AG to analyze a proposal and prepare a title and summary. According to the Consumer Price Index, the value of \$200 today is the equivalent of \$14.80 in 1943 dollars; the value of \$200 in 1943 translates to \$2,755 in 2015.²

Between 2009 and 2013, there were 315 proposed initiative measures submitted for a circulating title and summary, of which only 27 qualified for the ballot. The AG estimates that an average of 56 hours of staff time is spent preparing each title and summary.

System abuse?

AB 1100 is largely a response to recent ballot initiatives that seem to take advantage of California's very democratic ballot initiative system that allows voters to enact legislation. For example, initiatives have been submitted that call to ban alimony, create a secession commission, eliminate private power companies, fly the state flag above the national flag, and refer to the state's top elected official as the “president of California.”³ Specifically, it was an anti-gay initiative filed in February that was the main catalyst for AB 1100.

In its first draft, AB 1100 proposed raising the fee to \$8,000 — the amount estimated to cost the state to prepare an initiative's title and summary.⁴

AB 1100 opponents argued that raising the fee chips away at the state's democratic processes and curbs citizen participation.



¹ Elec. Code §9001

² Bureau of Labor Statistics CPI Inflation Calculator

³ www.capoliticalreview.com/tag/ab1100/

⁴ AB 1100 draft summary (March 24, 2015)

FTB's tax-sharing information program expanded

Big brother just got bigger — make sure your clients are complying with local licensing requirements.

By Sandy Weiner, J.D.
California Editor

AB 279 (Ch. 15-180) expands the FTB's current information sharing program with cities to allow disclosure between the FTB and counties as well, effective January 1, 2016.¹

Under the information sharing program, the FTB enters into agreements with cities, and beginning in 2016, with counties, to obtain their business licensing data to ensure compliance with state income tax requirements. At the same time, the cities use the FTB data to ensure that businesses located in their jurisdictions are complying with the city business tax requirements. The information sharing program is currently scheduled to expire on January 1, 2019.

The FTB anticipates that by expanding the program to include counties, the state will bring in up to \$800 million in 2017-18 when the program is fully phased in. The FTB anticipates that Sacramento County will join the program in the first year, Los Angeles and San Diego counties will join in the second year, and smaller counties will join in by the third year.²

Note: It's interesting that the FTB anticipates that San Diego County will join the program, as according to the San Diego County website, the county business license requirement was eliminated in 1998.

For information concerning the Sacramento County licensing requirements for businesses operating in unincorporated areas, see:

www.finance.saccounty.net/Tax/Pages/BusLicGeneral.aspx

Los Angeles County licensing requirements:

https://ttc.lacounty.gov/proptax/business_license.htm

San Diego County licensing requirements:

www.sandiegocounty.gov/content/sdc/cosd/businesslicenses.html

Background

Under the terms of the program, the FTB may only provide a city with tax data for taxpayers with an address within that city's or county's jurisdiction and is limited to the following data:

- Taxpayer name;
- Taxpayer address;
- Taxpayer Social Security number or taxpayer identification number; and
- Principal business activity code.

In addition, a city's or county's tax officials may request from the FTB any other taxpayer information but must do so by affidavit. At the time the tax official requests the tax information, he or she must provide a copy of the affidavit to the taxpayer whose information is sought, and upon request, make the obtained information available to that taxpayer.

The information sharing program has been a huge boost for cities, with cities reporting the following revenue amounts due to the program:³

- Los Angeles: \$13.9 million;
- San Diego: \$1.1 million;
- Newport Beach: \$360,000;
- Oakland: \$260,000;
- Menlo Park: \$172,000;
- Concord: \$154,000; and
- Sunnyvale: \$131,000

The information the FTB can request from cities is limited to the following:

- The name of the business if it is a corporation, partnership, or limited liability company, or the owner's name if it is a sole proprietorship;
- Business mailing address;
- Federal employer identification number, if applicable, or the business owner's Social Security number;
- Standard Industry Classification (commonly referred to as "SIC") code or North American Industry Classification System (commonly referred to as "NAICS") code;
- Business start date;
- Business termination date;
- City number; and
- Ownership type.

Compliance checks

There are currently 81 cities participating in the program, and the FTB attributes \$7.7 million in increased collections since the program's inception. Make sure as part of your annual client review process to inquire whether your business clients, including Schedule C filers, are current with their city business licenses. Remember that working out of the house does not exempt a taxpayer from licensing requirements. Acquaint yourself with the requirements for cities and counties in your area. Some local jurisdictions just require an annual fee, while others base their taxes on a percentage of gross revenues or income attributable to the locality.

Which Cities Are Participating?

Below is a list of California cities that receive business tax information from the FTB.

Alameda	Garden Grove	Salinas
Albany	Gilroy	San Bernardino
Alhambra	Hawaiian Gardens	San Bruno
Apple Valley	Hermosa Beach	San Carlos
Arcadia	Indio	San Diego
Bakersfield	Lodi	San Francisco
Bradbury	Los Angeles	San Jose
Brea	Martinez	San Juan Capistrano
Burlingame	Menifee	San Rafael
Carlsbad	Monrovia	Santa Ana
Carson	Montebello	Santa Cruz
Cathedral City	Moreno Valley	Santa Maria
Chino	Murrieta	Santa Monica
Cloverdale	Newport Beach	Seal Beach
Commerce	Norco	Solana Beach
Corona	Oakland	South Beach
Corte Madera	Oceanside	South Pasadena
Costa Mesa	Orange	South San Francisco
Delano	Pasadena	Sunnyvale
Downey	Paso Robles	Thousand Oaks
El Segundo	Pleasanton	Tustin
Emeryville	Pomona	Union City

Escalon	Rancho Cordova	Visalia
Escondido	Rancho Cucamonga	Ventura
Fontana	Rancho Palos Verdes	Vista
Fremont	Richmond	Walnut Creek
Fresno	Ridgecrest	West Covina



¹ R&TC §§19551.1, 19551.5

² FTB AB 279 Bill Analysis

³ AB 279, Legislative Bill Analysis, July 1, 2015

Did you know about Schedule EO?

The FTB wants LLCs and partnerships to report ownership of passthrough entities.

By Renée Rodda, J.D.

Editor

The FTB requires partnerships, LLCs taxed as partnerships, and/or those that own disregarded entities, including single-member LLCs, to complete the Schedule EO, Pass-Through Entity Ownership, to report all passthrough entities in which the taxpayer has an ownership interest. They wrote an article reminding taxpayers of this requirement in the September 2015 issue of FTB Tax News.¹

Although the schedules are required by the FTB, there is no penalty for failing to file them. Also, S corporations do not complete these schedules or use them to report passthrough income.

Comment

An S corporation can't be a member or partner, but an S corporation can own a partnership or an LLC.

What is on the form?

Schedule EO asks the taxpayer to identify name, Secretary of State number, and Federal Employer Identification Number (FEIN) for all partnerships (including LLCs taxable as partnerships), in which the taxpayer holds a partial interest, and for disregarded entities in which the taxpayer has full ownership. The information is requested regardless of whether the entities are required to file a tax return in California, or are subject to California annual tax or the LLC fee.

In addition, the FTB asks the taxpayer to indicate which entities received California-source income, and to provide the profit and loss sharing percentages used to compute the amount of income received by the owner.

Part I of Schedule EO asks for all partial ownership interests' profit and loss sharing percentages. Part II of Schedule EO asks for all 100% ownership interest information. Both ask for entity names, FEINs, and ownership percentages.

What is the purpose of the form?

The FTB states that they use this information to validate returns during processing, which they say significantly reduces processing time and errors. However, when you look at the

information they are requesting, it seems likely that they are using the information to help identify taxpayers they believe should be filing California returns.

It is no secret that the FTB has taken an aggressive position on LLCs taxed as partnerships, arguing that because all members can act on behalf of the LLC, all members are considered to be doing business in California if the LLC is doing business in California. This appears to be one more way to identify those taxpayers.



¹ "Schedule EO Forms," FTB Tax News (September 2015)

FTB will follow federal treatment of identity theft protection services

These noncash services are not included in gross income.

By **Sandy Weiner, J.D.**
California Editor

In IRS Announcement 2015-22, the IRS recently clarified its treatment of identity theft protection services provided to potential identity theft victims by businesses whose data has been breached.

The IRS stated that it "will not assert that":

- Individuals whose personal information may have been compromised in a data breach must include the value of the identity theft protection services in their gross income;
- Employers are required to include the value of the services provided to employees who might be victims of the data breach in the employee's gross income and wages; or
- Businesses are required to report these amounts on information returns (e.g., W-2s or 1099-MISC).

In other words, the IRS is essentially not requiring taxpayers to include these services in their gross income.

The FTB has stated that because the California Revenue and Taxation Code conforms to the federal definition of gross income in IRC §61, to the extent that the IRS is taking the position that the value of these services is not included in gross income, the FTB will follow that interpretation.

Limited relief

The IRS relief is limited and does not apply to:

- Cash received *in lieu* of identity protection services;
- Identity protection services received for reasons other than as a result of a data breach, such as identity protection services received in connection with an employee's compensation benefit package; or
- Proceeds received under an identity theft insurance policy.





No bill for sales tax on services this year — California's sales tax on services bill, SB 8 (Hertzberg), will not be enacted this year.

However, we expect that this new tax will probably return in some form next year, and we will keep you posted on any developments.

California Supreme Court denies Harley-Davidson's petition for review — The California Supreme Court denied Harley-Davidson's petition for review of a California appellate court decision finding that special purpose entity (SPE) subsidiaries used to support the taxpayer's financing business had California nexus even though the SPEs did not themselves have a physical presence in California.¹ The Supreme Court did not address the appellate court's separate finding that California's combined reporting scheme facially discriminates against interstate commerce. That portion of the decision was remanded back to the trial court to determine whether California can justify its discrimination under the Supreme Court's strict scrutiny test.

¹ *Harley-Davidson, Inc. v. FTB* (May 28, 2015) Cal.App., Case No. D064241, petition for review denied, California Supreme Court, Case No. S227652, September 16, 2015

More EDD and BOE relief for taxpayers affected by wildfires — Employers in Amador, Calaveras, Lake, and Napa counties directly affected by the series of wildfires may request up to a 60-day extension of time from the EDD to file their state payroll reports and/or deposit state payroll taxes without penalty or interest. Written request for extension must be received within 60 days from the original delinquent date of the payment or return to file/pay.

If you have any questions, contact the EDD's Taxpayer Assistance Center at:

(888) 745-3886

www.edd.ca.gov/Payroll_Taxes/Emergency_and_Disaster_Assistance_for_Employers.htm

The BOE has also extended emergency relief to taxpayers in these counties. That relief may include:

- Extended filing return dates;
- Relief of penalties and interest; or
- Replacement of copies of records lost.

For more information see BOE News Release NR 76-15-G (September 17, 2015) at:

www.boe.ca.gov/news/2015/76-15-G.htm

CALIFORNIA CONTACTS

To view the Roadmap to Understanding 2015 California Tax Legislation, go to:	www.caltax.com/spidellweb/public/editorial/2015CALegislation.pdf
For information concerning the Sacramento County licensing requirements for businesses operating in unincorporated areas, see:	www.finance.saccounty.net/Tax/Pages/BusLicGeneral.aspx
Los Angeles County licensing requirements:	https://ttc.lacounty.gov/proptax/business_license.htm
San Diego County licensing requirements:	www.sandiegocounty.gov/content/sdc/cosd/businesslicenses.html
Contact the EDD's Taxpayer Assistance Center at:	(888) 745-3886 or www.edd.ca.gov/Payroll_Taxes/Emergency_and_Disaster_Assistance_for_Employers.htm
For more information on emergency relief, see BOE News Release NR 76-15-G (September 17, 2015) at:	www.boe.ca.gov/news/2015/76-15-G.htm

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- Delve into case studies with completed A, B, & C trust allocations and funding documents
- Scrutinize A/B/C funding spreadsheet allocations
- Dig into the California Probate Code and uncover how it affects the funding process
- Use handy trust language examples to help you decipher the tax and funding clauses in your clients' trust documents

- Discover why words matter and how they affect the tax allocation and funding process outlined in the trust instrument
- Explore basis and step-up coverage, including the affect of title/ownership on after-death trust funding



Presented by Robert Manton, CPA

Robert is a partner with the firm McNally & Manton, CPAs Inc., serving the Orange County and Los Angeles areas for over 35 years. Estate and trust taxation has been his niche and specialty for over 20 years. He teaches estate and trust seminars, including in-house programs for large firms.

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 - Is there a standard format for reports?
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- Understand what items of taxable income actually must stay in the trust

- Discover when a dividend isn't income
- Wow! If something isn't income, does that mean you don't have to pay tax?



Larry A. Conway, CPA, Esq.

Larry Conway is a 1976 graduate of the University of Iowa, and practiced as a CPA for 26 years before obtaining his J.D. from California Western School of Law (magna cum laude) in 2003. While at California Western he served on the Law Review editorial board and received numerous scholarship awards in Taxation.

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- Review useful examples of grantor trust return preparation
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 - Find out why you might create a trust that is intentionally defective
 - See when an EIN is needed



Claudia Hill, EA, MBA

Claudia Hill is an enrolled agent, nationally recognized tax professional, and frequent lecturer on taxation of individuals, tax planning, and representation before the IRS. She is owner and principal of Tax Mam, Inc. and TMI Tax Services Group, Inc. in Cupertino, California.

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Burbank	Wednesday	October 28, 2015	Pickwick Gardens Conference Center
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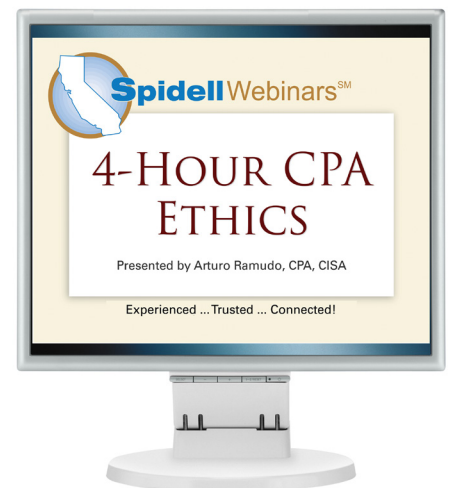
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Spidell's 2015/16 Federal and California Tax Update Seminar:

Day	Date	City	Venue	Day	Date	City	Venue
Monday	Nov. 16	Modesto	DoubleTree by Hilton Hotel Modesto	Monday	Jan. 4	Del Mar	Hilton San Diego/Del Mar
Monday	Nov. 16	San Luis Obispo	Embassy Suites San Luis Obispo	Monday	Jan. 4	Stockton	Hilton Stockton
Tuesday	Nov. 17	Bakersfield	DoubleTree by Hilton Hotel Bakersfield	Tuesday	Jan. 5	Sacramento	DoubleTree by Hilton Sacramento
Tuesday	Nov. 17	San Rafael	Embassy Suites San Rafael — Marin County	Tuesday	Jan. 5	Pasadena	Hilton Pasadena
Wednesday	Nov. 18	Oxnard	Residence Inn Oxnard River Ridge	Wednesday	Jan. 6	Costa Mesa	Hilton Orange County/Costa Mesa
Thursday	Nov. 19	Burbank	Pickwick Gardens Conference Center	Wednesday	Jan. 6	Santa Rosa	Hyatt Vineyard Creek Sonoma County
Friday	Nov. 20	Escondido	California Center for the Arts Escondido	Thursday	Jan. 7	Culver City	DoubleTree by Hilton Los Angeles — Westside
Monday	Nov. 23	City of Industry	Pacific Palms Resort & Conference Center	Thursday	Jan. 7	Berkeley	DoubleTree by Hilton Berkeley Marina
Monday	Nov. 30	Concord	Hilton Concord	Friday	Jan. 8	Milpitas	Embassy Suites Milpitas — Silicon Valley
Tuesday	Dec. 1	Sacramento	Crowne Plaza Sacramento Northeast	Monday	Jan. 11	Valencia	Hyatt Regency Valencia
Wednesday	Dec. 2	Culver City	DoubleTree by Hilton Los Angeles — Westside	Tuesday	Jan. 12	Westlake Village	Hyatt Westlake Plaza
Wednesday	Dec. 2	Rohnert Park	DoubleTree by Hilton Hotel Sonoma Wine Country	Wednesday	Jan. 13	Long Beach	Long Beach Marriott
Thursday	Dec. 3	Fresno	DoubleTree by Hilton Fresno Convention Center	Thursday	Jan. 14	San Ramon	San Ramon Marriott
Thursday	Dec. 3	So. San Francisco	South San Francisco Conference Center	Monday	Jan. 18	Sacramento	Crowne Plaza Sacramento Northeast
Friday	Dec. 4	Monterey	Embassy Suites Monterey Bay — Seaside	Tuesday	Jan. 19	Riverside	Riverside Convention Center
Monday	Dec. 7	Santa Barbara	The Fess Parker — A DoubleTree by Hilton Resort	Tuesday	Jan. 19	So. San Francisco	South San Francisco Conference Center
Tuesday	Dec. 8	Torrance	Torrance Marriott Redondo Beach	Wednesday	Jan. 20	San Diego	Scottish Rite Event Center
Friday	Dec. 11	San Jose	DoubleTree by Hilton San Jose	Thursday	Jan. 21	Burbank	Pickwick Gardens Conference Center
Monday	Dec. 14	San Diego	Scottish Rite Event Center	Friday	Jan. 22	Temecula	Pechanga Resort and Casino
Tuesday	Dec. 15	Rancho Mirage	Agua Caliente Casino Resort Spa	Monday	Jan. 25	Anaheim	Hilton Anaheim
Wednesday	Dec. 16	Burbank	Pickwick Gardens Conference Center	Tuesday	Jan. 26	San Jose	DoubleTree by Hilton San Jose
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 Live Webinar Times (2 days: 8:30 a.m. to noon Pacific Time)	Webinar 1	Webinar 2	Self-Study	
		Dec. 9 and Dec. 10	Jan. 14 and Jan. 15	Print (Available 12/1/15)

This seminar is designed to meet the requirements for 8 hours of continuing education for CPAs, PAs, and CFPs (CFPs do not receive credit for webinar or self-study versions of this course); 6 hours of Federal Update CPE for EAs, 6 hours of Federal Update and 2 CA for CRTPs, and 6.75 hours of General MCLE credit for attorneys. This seminar has been designed to meet the requirements of the IRS Return Preparer Office; including sections 10.6 and 10.9 of Department of Treasury's Circular No. 230 (Provider No. CRA7E); the California State Board of Accountancy; the California Bar Association; the Certified Financial Planner Board of Standards, and the California Tax Education Council. This does not constitute an endorsement by these groups. The state boards of accountancy have final authority on the acceptance of individual courses for CPE credit. For more information regarding administrative policies such as complaints or refunds, contact Spidell Publishing at 714-776-7850. A listing of additional requirements to renew tax preparer registration may be obtained by contacting CTEC at P.O. Box 2890, Sacramento, CA 95812-2890, or by phone at 877-850-2832, or on the internet at www.CTEC.org.



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