

# California

★ The Golden State ★



## GENERAL

Forms request	800-338-0505	
Tax assistance	800-852-5711 U.S.	916-845-6500 non U.S.
Website	ftb.ca.gov	
Refund information	800-338-0505 U.S.	916-845-6500 non U.S.

## NEW FOR 2014

**Voluntary contributions.** Taxpayers may contribute to the following new funds:

- California Senior Legislation Fund
- Habitat for Humanity Fund
- California Sexual Violence Victim Services Fund

**Premium assistance credit** which reduced the federal self-employed health insurance deduction may increase the deduction in California.

**Turf removal water conservation program.** Rebates, vouchers or other financial incentives issued by a local water agency or supplier can be excluded from gross income on Schedule CA.

**College access credit.** With a certificate from the California Educational Facilities Authority, a credit is available for contributions to the College Access Tax Credit Fund.

**Geographically targeted economic development area tax incentives** are repealed.

**New employment credit.** A credit is available for employers hiring qualified employees in a designated geographic area.

**California competes credit.** Tax credit available to businesses that want to come to California or stay and grow in California.

**Like-kind exchanges.** Annual information returns are required by taxpayers who exchange property located inside California for property located outside California.

## RESIDENCY STATUS

**Residents** include all individuals who are:

- In California for other than a temporary or transitory purpose or
- Domiciled in California, but outside California for a temporary or transitory purpose.

A resident who is outside California for a temporary or transitory purpose remains a resident.

**Part-year residents** are California residents for part of the year and nonresidents for part of the year.

**Nonresident.** Any individual who is not a resident.

**Safe harbor.** Individuals domiciled in California who are outside California under an employment-related contract for at least 546 consecutive days will be considered a nonresident unless:

- The individual has intangible income exceeding \$200,000 in any year the employment contract is in effect.
- The principal purpose of absence is tax avoidance.

Return visits to California that in the aggregate do not exceed 45 days during the tax year are considered temporary. See FTB Publication 1031 for more information.



**Military.** An individual domiciled in California when entering the military is considered a:

- Resident while stationed in California.
  - Resident while stationed in California on permanent change of station (PCS) orders and temporary duty (TDY) assignments outside California, regardless of duration.
  - Nonresident while stationed outside California on PCS orders.
- Military members domiciled outside California are considered nonresidents for tax purpose even when stationed in California unless they establish a California domicile. See FTB Publication 1032 for more information.

## FILING REQUIREMENTS

**Residents, part-year and nonresidents.** A return must be filed if either California gross income or California AGI is more than the amount shown in the tables below.

California gross income exceeds:			
Number of dependents:	0	1	2 or more
Single or HOH under age 65	\$16,047	\$27,147	\$35,472
Single or HOH age 65 or over	21,447	29,772	36,432
Married/RDP <sup>1</sup> under age 65 (both)	32,097	43,197	51,522
Married/RDP <sup>1</sup> age 65 or over (one)	37,497	45,822	52,482
Married/RDP <sup>1</sup> age 65 or over (both)	42,897	51,222	57,882
QW under age 65	N/A	27,147	35,472
QW age 65 or over	N/A	29,772	36,432
Or, California adjusted gross income exceeds:			
Number of dependents:	0	1	2 or more
Single or HOH under age 65	\$12,838	\$23,938	\$32,263
Single or HOH age 65 or over	18,238	26,563	33,223
Married/RDP <sup>1</sup> under age 65 (both)	25,678	36,778	45,103
Married/RDP <sup>1</sup> age 65 or over (one)	31,078	39,403	46,063
Married/RDP <sup>1</sup> age 65 or over (both)	36,478	44,803	51,463
QW under age 65	N/A	23,938	32,263
QW age 65 or over	N/A	26,563	33,223

<sup>1</sup> Whether filing jointly or separately. The income of both spouses (or RDPs) must be combined.

A dependent, any age, any filing status, must file if income is more than the standard deduction for the dependent.

California conforms to the federal rules for the "kiddie tax." Each child who is 18 and under or each full-time student under age 24 receives more than \$2,000 of investment income must complete Form 540 and Form FTB 3800 to figure tax. Or, if the child's income is \$10,000 or less (but not less than \$1,000), the parent may elect to report the child's income on the parent's return by completing Form FTB 3803.

Individuals who owe any of the following taxes must also file.

- Tax on a lump-sum distribution.
- Tax on a qualified retirement plan, IRA or Archer medical savings account (MSA).
- Tax for children under age 19 or students under age 24 who have investment income greater than \$2,000.
- Alternative minimum tax (AMT).

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# California

- Recapture taxes.
- Deferred tax on certain installment obligations.
- Tax on an accumulation distribution from a trust.

## FORMS TO FILE

**Form 540**, *California Resident Income Tax Return*. For residents.

**Schedule CA (540)**, *California Adjustments—Residents*. Attachment to Form 540 used to report additions, subtractions and adjustments to income, and adjustments to federal itemized deductions.

**Form 540NR**, *California Nonresident or Part-Year Resident Income Tax Return*. For part-year residents and nonresidents.

**Schedule CA (540NR)**, *California Adjustments—Nonresidents or Part-Year Residents*. Attachment to Form 540NR used to report additions, subtractions and adjustments to income, and adjustments to federal itemized deductions. Also used to compute the California income ratio used to compute tax for part-year and nonresidents.

**Schedule D (540)**, *California Capital Gain or Loss Adjustment*.

**Schedule D (540NR)**, *California Capital Gain or Loss Adjustment*.

**Form 540-ES**, *Estimated Tax for Individuals*.

**Form 3506**, *Child and Dependent Care Expenses Credit*.

**Form 3519**, *Payment for Automatic Extension for Individuals*.

**Form 3885A**, *Depreciation and Amortization Adjustments*.

## FILING STATUS

California filing status must be the same as federal filing status (including same-sex married couples).

### Exceptions:

- 1) Couples who file a joint federal return may file either MFJ or MFS if either spouse is active military or a California nonresident with no California-source income. Community property laws must be considered if domiciled in such a state.
- 2) Individuals who have entered into a registered domestic partnership (RDP) or a similar same-sex legal union in another state must file either married/RDP filing jointly or married/RDP filing separately, rather than as single. A taxpayer in such a partnership may file as head of household (HOH) only if he meets the requirements to be considered not in a domestic partnership.
- 3) To qualify for HOH, the taxpayer must have been unmarried or not in an RDP (or met the requirements to be considered such on December 31, 2014). For more than half the year, the taxpayer's home must have been the main home for a qualifying individual. The taxpayer must not have been a nonresident alien at anytime during the year. See FTB Pub. 1540, *California Head of Household Filing Status*, for the specific requirements that must be met.

## RESIDENT SUMMARY

Form 540

**Principal business activity (PBA) code.** Include the PBA code from line B of federal Schedule C.

**Additional information field.** Additional information (such as "in-care-of" name or other supplemental address information) can be entered into this field.

**Prior name.** Include the last name from the 2013 tax return if different in 2014.

## Exemptions

See *Exemptions* on Page CA-8.

## Adjusted Gross Income

California starts with federal AGI. Registered domestic partners (RDPs) who file a California return as Married/RDP filing jointly and have no filing status adjustments will need to combine their federal adjusted gross incomes. If they do have filing status adjustments, they will need to complete:

- 1) The California RDP Adjustments Worksheet in FTB Pub. 737, *Tax Information for Registered Domestic Partners* or
- 2) A federal pro-forma Form 1040.

Filing status adjustments include (but are not limited to) capital loss limitations, transactions between the spouses/RDPs, passive loss limitations, interest on student loans, investment interest expense and dependent care assistance.

**Note:** Throughout this state tab, the abbreviations MFJ or MFS will include RDPs who file jointly or separately.

## Adjustments—Schedule CA (540)

Use this schedule to make adjustments to federal AGI and to federal itemized deductions using California law.

**Column A.** Enter on lines 7 through 36 the same amounts that are entered on lines 7 through 36 of federal Form 1040.

Also enter the following if applicable:

- The tax-exempt interest received on line 8b,
- The total ordinary and qualified dividends received on line 9b,
- The total IRA distribution received on line 15a,
- The total pension or annuity distribution received on line 16a and
- The total Social Security retirement benefit received on line 20a.

**Columns B and C.** Use these columns to enter subtractions (column B) and additions (column C) to the federal amounts in column A that are necessary because of differences between California and federal law. Enter all amounts as positive numbers unless instructed otherwise. The total for line 37, column B, should be entered on line 14 of Form 540. The total for line 37, column C, should be entered on line 16 of Form 540. However, if the total for line 37, column B, is a negative number, transfer the amount as a positive number on line 16 of Form 540. And if the total for line 37, column C, is a negative number, transfer the amount as a positive number on line 14 of Form 540.

**Note:** FTB Pub. 1001 contains detailed information on the differences between California AGI and federal AGI, which require adjustments on Schedule CA. Following is a summary of reporting some of the more common adjustments.

## Line 7—Wages, Salaries, Tips, etc.

**Military pay adjustment (MPA).** Special rules apply to active duty military pay taxpayers. See FTB Pub. 1032 for details.

**Sick pay.** Federal taxable sick pay received under the Federal Insurance Contributions Act (FICA) and Railroad Retirement Act should be in column B.

**Ridesharing fringe benefits.** Under federal law, qualified transportation benefits are excluded from gross income. Under California law, there are no monthly limits for the exclusion of these benefits and California's definitions are more expansive. Enter any ridesharing benefits that are included in federal taxable income in column B.



# California

**Qualified stock option.** Exercising a California qualified stock option (CQSO) is not taxable if:

- 1) Earned income from the corporation granting the CQSO is \$40,000 or less,
- 2) The market value of the options granted is less than \$100,000,
- 3) The total number of shares is 1,000 or less and
- 4) The corporation issuing the option designates that the stock qualifies as a CQSO at the time the option is granted.

If an amount qualifying for this exclusion was included in federal income, enter that amount in column B.

**Other wage adjustments.** Other potential wage adjustments include:

- Employer health savings account contribution from Form W-2, box 12, code W. (Column C)
- Income exclusion for employer-provided adoption benefits from federal Form 8839, up to \$1,000. (Column C)
- Federally tax-free medical coverage of non-dependent adult children. (Column C)
- Income exempted from the federal return by tax treaty unless the treaty specifically excludes the income from state taxation. (Column C)
- Earnings of American Indians from reservation sources. (Column B)
- Clergy housing exclusion for rental allowances in excess of the fair rental value of the home. (Column B)
- Housing exclusion for state-employed clergy, if different from federal amount. (Column B if California exclusion is larger, Column C if smaller)
- Nonresident employee compensation of merchant seamen, rail carriers, motor carriers, and air carriers. (Column B)

## Line 8—Taxable Interest

The following taxable interest for federal purposes should be subtracted on the California return (Column B):

- U.S. government interest. Do not make any adjustment for interest income from the Federal National Mortgage Association (Fannie Mae), the Government National Mortgage Association (Ginnie Mae), or the Federal Home Loan Mortgage Corporation (FHLMC).
- Loans made to a business located in an enterprise zone. Complete Form FTB 3805Z.
- Interest income from settlement payments from the Ottoman Turkish Empire.
- Interest income from children under age 19 or full-time students under age 24 included on the child's federal tax return and reported on the California tax return by the parent.
- The amount of *exempt-interest* mutual fund distributions attributable to U.S. obligations and included in federal taxable income, provided the mutual fund has at least 50% of its assets invested in tax-exempt U.S. obligations and/or in California or its municipal obligations.

The following tax-exempt interest for federal purposes must be added back (reported in Column C):

- Non-California state bonds.
- Non-California municipal bonds.
- Obligations of the District of Columbia issued after December 27, 1973.
- Non-California bonds if the interest was passed through from an S corporation, trust, partnership or limited liability company (LLC).
- Interest or other earnings earned from a health savings account (HSA).
- Government of American Samoa bonds.

- Interest income from children under age 19 or full-time student under age 24 included on the parent's federal tax return and reported on the California tax return by the child.
- Federally exempt mutual fund distributions attributable to obligations of other states and their municipalities or from mutual funds that do not have at least 50% of their assets invested in tax-exempt U.S. obligations and/or in obligations of California or its municipal obligations.

## Line 9—Ordinary Dividends

The following dividend income included in federal taxable income is a subtraction (reported in column B):

- The portion of dividends from mutual funds that represents U.S. government interest, but only if the mutual fund has at least 50% of its assets invested in tax-exempt U.S. obligations and/or in California or its municipal obligations.
- Non-cash patronage dividends from farmers' cooperatives or mutual associations.
- Dividend income received by children under age 19 and students under 24 included on the parent's or child's federal tax return and reported on the California tax return by the opposite taxpayer.

The following dividend income that is exempt from federal tax is an addition (reported in column C):

- The portion of dividends from mutual funds that represents municipal obligations from other states and/or California municipal obligations if the mutual fund does not meet the 50% rule previously mentioned.
- Controlled foreign corporation dividends in the year distributed.
- Regulated investment company (RIC) capital gains in the year distributed.
- Distributions of pre-1987 earnings from an S corporation.
- Dividend income from children under age 19 or full-time students under age 24 excluded on the parent's or child's federal tax return and reported on the California tax return by the opposite taxpayer.

## Line 10—State Tax Refund

The state income tax refund received in 2014 that is included in column A is a subtraction in column B.

## Line 11—Alimony Received

If the taxpayer is a nonresident alien and received alimony that was not included in federal income, enter the alimony in column C as an addition.

## Line 12—Business Income (or Loss)

Adjustments to federal business income or loss reported in column A generally are necessary because of the difference between California and federal law relating to depreciation methods, special credits and accelerated write-offs. As a result, the recovery period or basis used to figure California depreciation may be different from the amount used for federal purposes.

Adjustments are figured on Form FTB 3885A, *Depreciation and Amortization Adjustments*, and are most commonly necessary because of the following.

- Before January 1, 1987, California did not allow depreciation under the federal accelerated cost recovery system. Continue to figure California depreciation for those assets in the same manner as prior years.
- On or after January 1, 1987, California provides special credits and accelerated write-offs that affect the California basis of qualifying assets.

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# California

- California does not presently conform to the additional first-year bonus depreciation provisions allowed for federal purposes.

Use Form FTB 3801, *Passive Activity Loss Limitation*, to figure the total adjustment for line 12 if taxpayer has:

- One or more passive activities that produce a loss or
- One or more passive activities that produce a loss and any non-passive activity reported on federal Schedule C.

Use Form FTB 3885A to figure the total adjustment for line 12 if taxpayer has:

- Only nonpassive activities that produce either gains or losses (or combination of gains and losses) or
- Passive activities that produce gains.

Adjustments may also be necessary for income related to:

- Business, trade or profession carried on within California that is an integral part of a unitary business carried on both within and outside California or
- Pro rata share of income received from a controlled foreign corporation by a U.S. shareholder.

Basis adjustments may also be necessary for:

- Property acquired prior to becoming a California resident.
- Sales or use tax credit for property used in an enterprise zone (EZ), local agency military base recovery area (LAMBRA), targeted tax area (TTA) or former Los Angeles Revitalization Zone (LARZ).
- Reduced recovery periods for fruit-bearing grapevines replaced in a California vineyard on or after January 1, 1992, as a result of phylloxera infestation, or on or after January 1, 1997, as a result of Pierce's disease.
- Expenditures for tertiary injectants.
- Property placed in service on an Indian reservation after January 1, 1994, and before January 1, 2014.
- Amortization of pollution control facilities.
- Discharge of real property business indebtedness.
- Vehicles used in an employer-sponsored ridesharing program.
- An enhanced oil recovery system.
- Joint Strike Fighter property costs.
- The cost of making a business accessible to disabled individuals.
- Property for which taxpayer received an energy conservation subsidy from a public utility on or after January 1, 1995, and before January 1, 1997.
- Research and experimental expenditures.

Adjustments may be necessary for business expense deductions related to:

- Wages paid in an EZ, LAMBRA, manufacturing enhancement area (MEA) or TTA.
- Certain employer costs for employees who are also enrolled members of Indian tribes.
- Abandonment or tax recoupment fees for open-space easements and timberland preserves.
- Research expense.
- Employer wage expense for the work opportunity credit.
- Pro rata share of deductions received from a controlled foreign corporation by a U.S. shareholder.
- Interest paid on indebtedness in connection with company-owned life insurance policies.
- Premiums paid on life insurance policies, annuities or endowment contracts issued after June 8, 1997, where the owner of the business is directly or indirectly a policy beneficiary.
- Commercial revitalization deduction for renewal communities.
- Small employer health insurance credit.

## Line 13—Capital Gain (or Loss)

An adjustment may be needed for the items below. Use Schedule D, *California Capital Gain or Loss Adjustment*, to calculate the amount to enter on line 13.

- Gain on the sale of qualified small business stock under Section 1045 or Section 1202 of the Internal Revenue Code.
- Basis amounts resulting from differences between California and federal law in prior years.
- Gain or loss on stock and bond transactions.
- Installment sale gain reported on Form FTB 3805E, *Installment Sale Income*.
- Gain on the sale of personal residence where depreciation was allowable.
- Flow-through gain or loss from partnerships, fiduciaries, S corporations or LLCs.
- Capital loss carryover from 2013 California Schedule D.
- Capital gain earned by a child under age 19 or a full-time student under age 24 included on the parent's or child's federal return and reported on the California return by the opposite taxpayer.



Other adjustments may be needed for the following:

- Disposition of S corporation stock acquired before 1987.
- Capital gain exclusion for sale of principal residence by a surviving spouse.
- Gain on sale or disposition of qualified assisted housing development to low-income residents or to specified entities maintaining housing for low-income residents.
- Undistributed capital gain for RIC shareholders.
- Gain or loss on the sale of property inherited before January 1, 1987.
- Capital loss carrybacks.

## Line 14—Other Gains (or Losses)

California basis of other assets may be different from the federal basis due to differences between California and federal law. See Schedule D-1, *Sales of Business Property*.

## Line 15—IRA Distributions

There may be differences in the taxable amount of a distribution (including a distribution from conversion of a traditional IRA to a Roth IRA) depending on when contributions to the IRA were made. Differences may also occur if California IRA deductions were different from federal deductions because of differences between California and federal self-employment (SE) income. If taxpayer has an IRA basis and was a nonresident in prior years, California IRA basis may need to be restated. See FTB Pubs. 1005 and 1100 for more information.

## Line 16—Pensions and Annuities

If a taxpayer received Tier 2 railroad retirement benefits or partially taxable distributions from a pension plan, make the following adjustments.

- Railroad retirement benefits from federal Form RRB 1099-R included in column A should be entered in column B.
- If the taxpayer began receiving a retirement annuity between July 1, 1986, and January 1, 1987, and elected to use the three-year rule for California purposes and the annuity rules for federal purposes, enter in column C the amount of the annuity payments that were excluded for federal purposes.