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California does not conform to OBBBA changes

New adjustments are coming for the 2025 tax year.

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

Because California only currently conforms to the Internal Revenue Code as in effect on January 1, 2015, California will not automatically conform to any of the changes made by the One Big, Beautiful Bill Act (OBBBA; P.L. 119-21 (H.R. 1)). This would be true even if SB 711 is enacted as currently written, which would update California's conformity specified date from January 1, 2015, to January 1, 2025, because OBBBA was not enacted until July 4, 2025.

Note: While SB 711 would, if enacted, update California's conformity specified date to January 1, 2025, generally, many of SB 711's provisions would specifically not conform to most of the significant changes made by the TCJA. See "Conformity legislation introduced" in the May 2025 issue of *Spidell's California Taxletter*®.

Due to California's current nonconformity to the tax changes made by OBBBA, there will be additional adjustments required on the 2025 California return including adjustments for:

- The senior personal exemption deduction;
- The qualified tip deduction;
- The qualified overtime deduction;

- The deduction for interest on qualifying passenger vehicle loans;
- The enhanced personal casualty losses for disaster victims (see below); and
- The tax-free treatment of withdrawals from §529 plans to cover qualified credential program expenses and additional K-12 school expenses.

Disaster relief

As a result of changes made by OBBBA, Los Angeles wildfire victims now qualify for the following enhanced personal casualty deductions applicable to “qualified disaster losses” on their federal tax returns:

- The 10% AGI floor on net casualty losses is not applicable, but the \$100 per-casualty limit is increased to \$500; and
- Nonitemizers can claim the personal casualty loss.

While these changes apply on the federal return, California does not currently conform, meaning the 10% floor and the \$100 per-casualty limit still apply on the California return, and nonitemizers cannot claim the personal casualty loss.

Business tax provisions

Remember that California never conformed to bonus depreciation, increased §179 expense amounts, the business interest limitation, or the qualified small business stock exclusion (at least in recent years), so adjustments continue to be required for these items.

However, because California never conformed to the TCJA's requirement that taxpayers amortize research expenses, OBBBA's reinstatement of current expensing for domestic research expenses may actually result in one less adjustment on the California return.

We will be covering all the conformity issues that will arise due to OBBBA in Spidell's 2025/2026 Federal and California Tax Update.



Budget deal contains welcome relief for many taxpayers

A retroactive wildfire settlement exclusion and retirement pay exclusions for uniformed federal employees are among changes enacted.

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

SB 132 (Ch. 25-17), which was a part of the budget deal reached between the Governor and the Legislature, enacts several new tax provisions, many of which are taxpayer-friendly. We cover the changes made to the passthrough entity elective tax in the article “Big changes coming to California's passthrough entity tax” in this issue. Other highlights of the bill are discussed below.

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Federal uniformed retirement pay exclusion

Effective for the 2025 through 2029 taxable years, a new gross income exclusion is available for up to \$20,000 of retirement pay paid to qualified individual taxpayers from the federal government for service in the following uniformed services:

- U.S. Armed Forces;
 - Army National Guard and the Air National Guard when engaged in active duty for training, inactive duty training, or full-time National Guard duty;
 - The commissioned corps of the U.S. Public Health Services; and
 - The National Oceanic and Atmospheric Administration (NOAA) Commissioned Officer Corps.
- (R&TC §17132.9)

A similar exclusion also applies to annuity payments received by California taxpayers from a U.S. Department of Defense Survivor Benefit Plan. (R&TC §17132.10)

Taxpayers can only qualify for these exclusions if their federal AGI for the taxable year does not exceed \$125,000 (\$250,000 for MFJ and surviving spouses).

Wildfire settlement exclusion

In addition, a retroactive personal income tax and gross income exclusion is available for the 2022 through 2029 taxable years for amounts received by qualified taxpayers from a class action settlement in connection with a California wildfire.

For purposes of this exclusion, qualified taxpayers are those listed below who received class action settlements to cover wildfire-related expenses:

- Any taxpayer who owns real property located in an area damaged by a wildfire;
 - Any taxpayer who resides within an area damaged by a wildfire; and
 - Any taxpayer who has a place of business within an area damaged by a wildfire.
- (R&TC §§17138.7, 24309.2)

Previously, California had provided a patchwork of relief related to various wildfires. This new exclusion will cover all wildfire settlements received going back to the beginning of the 2022 taxable year that were not previously covered, as well as the Los Angeles wildfires in early 2025.

Exclusion for Chiquita Canyon landfill victims

Retroactive tax relief is also available for payments related to the Chiquita Canyon elevated temperature landfill event in Los Angeles County that began in May 2022. (R&TC §§17157.5, 24309.9)

Effective for the 2024 through 2028 taxable years, corporation franchise and income tax taxpayers may exclude payments received on or after March 1, 2024, as compensation for loss, damages, expenses, relocation, suffering, loss in real property value, closing costs with respect to real property (including realtor commissions), or inconvenience, including access to real property. The excludable payments must be paid from:

- A federal, state, or local government agency; and/or
- Waste Connections, Inc., any subsidiary, insurer, or agent of Waste Connections, Inc., or any person related to Waste Connections, Inc.

California Film and Tax Credit Program 4.0 funding increase

The amount of credits available annually for allocation to taxpayers approved for the California Film and Tax Credit Program 4.0 is increased from \$330 million to \$750 million for the 2025–26 through 2029–30 fiscal years. (R&TC §23698.1)

Apportionment formula for financial institutions

Beginning with the 2025 taxable year, certain financial institutions must use a single sales factor formula rather than a three-factor (property, payroll, and sales) formula to apportion

their business income to California. (R&TC §25128) This applies to financial institutions involved in a savings and loan activity or banking or financial business activity.



Big changes coming to California's passthrough entity elective tax

The passthrough entity tax has been extended and the June 15 prepayment requirement eased.

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

As part of this year's budget deal, SB 132 (Ch. 25-17) extends the availability of the California passthrough entity tax election for an additional five years, with modifications. This means that qualified passthrough entities will be able to make the election during the 2026 through 2030 tax years. (R&TC §19916)

June 15 prepayment requirement eased

For taxable years prior to 2026, an entity is prohibited from making the election for the tax year if it fails to pay by June 15 of the current tax year the greater of:

- \$1,000; or
- 50% of the amount of the passthrough entity tax due for the prior year.

This has resulted in many entities being unable to make the election if they are even a day late or a dollar short of these requirements, literally.

As a result of changes made by SB 132, this will no longer be the case, effective for the 2026 through 2030 taxable years. Beginning with the 2026 tax year, passthrough entities will still be able to make a passthrough entity tax election even if they don't timely meet the June 15 prepayment requirement. (R&TC §19914(b)) This relief is not available for the 2025 taxable year if the taxpayer failed to comply with the prepayment requirement by June 15, 2025.

The ability to make the election even if the June 15 requirements are not met comes at a cost. If the June 15 payment is late or underpaid, the credit that the individual, trust, estate, or qualified SMLLC owners can claim will be reduced by 12.5% of the amount underpaid by the June 15 prepayment due date. (R&TC §17052.11(2)(B))

For example, if a partnership with two 50% individual partners underpays its June 15 prepayment for the 2026 tax year by \$20,000, the \$10,000 credit that each partner would be entitled to claim on their 2026 return would be reduced by \$1,250. In effect, the 12.5% reduction of the credit acts as a late-payment penalty imposed directly against the owners.

Fiscal-year taxpayers

The bill also clarifies when the entity's owners that are eligible to claim the Passthrough Entity Elective Tax Credit can claim the credit for a fiscal-year entity that files its return for their taxable year beginning on or after January 1, 2025, and before January 1, 2026. These owners should claim the credit on their 2026 taxable year return (for calendar-year taxpayers).

Interplay with federal SALT limitation

Similar to the passthrough entity tax provisions that were in effect during the 2021 through 2025 taxable years, the availability of the election for the 2026 through 2030

taxable years is dependent on the IRC §164(b) SALT deduction limitation remaining in place, regardless of the limitation amount. (R&TC §19916(c)) The fact that the maximum SALT deduction has increased from \$10,000 (\$5,000 MFS) to \$40,000 (\$20,000 MFS) has no impact on the availability of the California passthrough entity tax.

Should IRC §164(b) be repealed and a full SALT deduction allowed on the federal return, California's passthrough entity tax would be repealed for taxable years beginning on or after January 1 of the year in which the federal SALT limitation is repealed. (R&TC §19916(c)) However, even if the passthrough entity tax is repealed, the five-year carryover of unused Passthrough Entity Elective Tax Credits would still be available, meaning that carryover credits from taxable years prior to the passthrough entity tax repeal would still be available for the balance of the five-year carryover period.

Overview of California's passthrough entity elective tax

Under California's passthrough entity tax regime, S corporations, partnerships, and LLCs taxed as an S corporation or partnership may elect to pay 9.3% of their qualified business income attributable to their consenting individual, estate, or trust owners (or an SMLLC owned by an individual, trust, or estate). For the law in effect for pre-2026 tax years, the entity can only make the election if it complies with the June 15 prepayment requirement discussed above.

The tax is fully deductible on the entity's federal return for the tax year in which the payment is made. Although the tax is added back on the California return, consenting owners can claim a nonrefundable credit of up to 100% of their share of the tax paid by the entity in the year the entity makes the election (87.5% for entities that miss or underpay the required June 15 prepayment starting with the 2026 taxable year). Unused credit can be carried over for five taxable years and is claimed on a first-in, first-out basis.



Responding to FTB notices

Here are some tips for the most efficient ways to respond to FTB notices.

By Kathryn Zdan, EA
Contributing Editor

This is the time of year during which the FTB begins sending notices to taxpayers stemming from the returns and payments processed from the previous filing season. ("Ask the Advocate: Expect notices to go out soon!" FTB Tax News (July 2025)) If a taxpayer receives a notice, the most efficient way to address the issue is to follow the instructions on the notice.

The top three notices that the FTB receives calls about are:

1. **FTB 4601, Demand for Tax Return:** Issued when the FTB has no record of a filed tax return. If the taxpayer does not file by the due date shown (or explain why they do not have a filing requirement), the FTB may issue a proposed assessment based on estimated income from third-party sources;
2. **FTB 4963, Notice of State Income Tax Due:** Reflects the current balance due including tax, penalties, and interest that result from a filed or adjusted tax return; and
3. **FTB 5818, Notice of Tax Return Change:** Sent when the FTB adjusts a filed tax return due to identified discrepancies, data mismatches, or missing information.

Dealing with notices online

The FTB maintains a list of all notices with information on how to respond:

www.ftb.ca.gov/help/letters/index.html

Tax professionals can respond to a client's notice through MyFTB's Secure Message service using the "Send Message to FTB" from the Communication tab after selecting the taxpayer from the client list. When using this method of communication, MyFTB will automatically keep the documents together to ensure accurate processing.

Also, the FTB's new online self-service tool Personal Income Tax Self-Correct allows taxpayers to respond online to, FTB 5818, Notice of Tax Return Change, when Form FTB 3514, California Earned Income Tax Credit, is missing. Taxpayers can respond through their MyFTB account with the unique URL provided on the notice received or by mailing Form 3514 to the address indicated on the notice.

If the client's notice cannot be resolved through online self-service options, call the number provided on the notice because this number will connect directly with the appropriate FTB unit.

Erroneous disaster notices

If a taxpayer was a victim of the Los Angeles County wildfires and qualified for October 15, 2025, filing and payment postponement, use the contact information below if the taxpayer received an erroneous notice from the FTB:

FTBLACountyDisasterRelief@ftb.ca.gov

(888) 825-9868

www.ftb.ca.gov/myftb/index.asp

Don't miss a notice

To stay informed about client notices, the FTB encourages tax professionals to:

- Register for a MyFTB account and request full online access;
- Include an e-mail address on POA declarations to be notified when a new client notice is available;
- Review notices carefully and access MyFTB to confirm account activity;
- Promptly communicate with clients to explain the notice and any required action;
- Respond to the FTB within the specified time frame to preserve protest or appeal rights and prevent adverse collection activity; and
- Remind clients to keep their contact information and address updated with the FTB.

FTB notices survey

The FTB has created a survey to gather valuable feedback for potential improvements to FTB notices. The survey only takes a few minutes to complete, and participants have the option to remain anonymous.

You can access the survey here.

<https://bit.ly/tax-news-survey>



When manufacturer rebates are included in gross receipts

Documentation provides the taxpayer a partial win.

By Kathryn Zdan, EA
Contributing Editor

A boat retailer was able to successfully show that payments from a manufacturer were not includable in gross receipts for the purposes of calculating sales and use tax. (*Appeal of Sails By Schock*, 2025-OTA-428)

The taxpayer received payments from two boat manufacturers, Grady-White and Boston Whaler, which the taxpayer used to reduce the selling price of the boats. During audit, the CDTFA determined that these manufacturer payments were offered on a transaction-by-transaction basis and were therefore includable in gross receipts. The CDTFA determined that the taxpayer had not reported \$77,250 in rebates and assessed \$6,358 in sales tax.

Rebate programs, generally

Under certain conditions, payments received by a retailer in the form of rebates or other types of payments or credits for products sold at retail are included in the retailer's gross receipts. (18 Cal. Code Regs. §1671.1(a))

When a retailer enters into an oral or written contract with a manufacturer or other third party that requires, on a transaction-by-transaction basis, a specific reduction in the retailer's selling price of specified products in exchange for a certain payment of a like amount from the contracting party (e.g., a payment that is not contingent upon selling a particular amount of the specified products), such payments received by the retailer are part of the taxable gross receipts or sales price of the sales. (18 Cal. Code Regs. §1671.1(c)(3)(A))

However, this is a rebuttable presumption. In order to rebut the presumption that the rebates are included in gross receipts for sales tax purposes, the retailer must provide any of the following documentation:

- A copy of an agreement or contract between the retailer and a third party that requires the retailer to give specified products preferential shelf space or to display the products in specific areas of the retailer's establishment in exchange for the payment received;
 - A copy of an agreement or contract between the retailer and a third party that provides the retailer with an advertising allowance, equal to or in excess of the payment received, when the retailer advertises the third party's products; or
 - A copy of an agreement or contract between the retailer and a third party that provides that the retailer will only receive the payment if the retailer sells a certain quantity of the products within a specified price range during a particular period, or if the retailer purchases a certain quantity of the products during a particular period.
- (18 Cal. Code Regs. §1671.1(c)(3)(A)(1)–(3))

OTA sinks CDTFA's arguments

The taxpayer argued that the payments it received from Grady-White and Boston Whaler were not subject to sales tax because it did not have contracts with the manufacturers that required the taxpayer to reduce the selling price of the boats in order to receive the payments.

As proof, the taxpayer provided two letters from Grady-White, signed by the vice president of sales, stating that:

- Dealers are not required to reduce the selling price of their boats to receive the promotional allowances;
- Grady-White has no control over the selling price offered by the dealer;
- The selling price of a boat has no impact on the receipt of any promotional allowance; and
- Dealers are not required to extend the promotion to customers. Dealers have discretion as to how to process the money upon receiving the promotional allowance.

The taxpayer did not have similar letters from Boston Whaler but argued that the same fact pattern applied to that rebate program.

The CDTFA argued that the taxpayer didn't provide any contracts or written materials outlining the rebate programs, only the two letters and a promotion announcement from Grady-White. The CDTFA called into question the authenticity of the letters because they were obtained after the audit had begun. The CDTFA also argued that the taxpayer used the promotional allowances to reduce the selling price of the boats by the same amount.

However, the OTA accepted the manufacturer letters, noting that they are similar to XYZ letters, which are used to show that sales in question were nontaxable resales — both XYZ letters and the manufacturer letters in this appeal generally only need to be obtained when a taxpayer is under audit. The OTA also pointed out that the CDTFA did not make any attempt to verify the information in the letters, despite having the opportunity to do so.

The OTA also held that reducing the sales price of the boats by the promotional allowances did not make the payments subject to sales tax. The OTA cited CDTFA Annotation 295.0948, which notes that in some situations, the taxpayer may pass on the reduction to the consumer dollar for dollar.

Because the CDTFA did not provide evidence that the taxpayer was required to reduce the selling price of the boats, the promotional allowances from Grady-White were not subject to sales tax. However, because the taxpayer did not have any evidence such as letters or promotional flyers for Boston Whaler (the taxpayer only argued that the program was the same as Grady-White), those payments were subject to sales tax.



Student gets tax bill for crypto trading activities

Cryptocurrency may not be “real” in the physical sense, but it’s certainly not Monopoly money.

By Kathryn Zdan, EA
Contributing Editor

A taxpayer was liable for tax, penalties, and interest on unreported proceeds from the sale of cryptocurrency stemming from cryptocurrency trading activities. (*Appeal of Guedikian*, 2025-OTA-420)

The taxpayer never filed a 2020 tax return. In January of 2024, the FTB used information received from the IRS from that tax year to estimate income of over \$1.5 million and issued a Notice of Proposed Assessment. Without filing Forms 1040 or 540, the taxpayer submitted

a *pro forma* 2020 Schedule D, 2020 Form 8949, and a spreadsheet to indicate he had received \$2.3 million in short-term proceeds, but had a basis of \$2.4 million, for a net short-term capital loss.

At appeal, the taxpayer argued that he did not receive payments of over \$1.5 million for 2020. He argued that he was a medical student during that tax year, and he had used his loan and COVID-19 relief funds to trade cryptocurrency but otherwise had minimal income. The taxpayer's argument was that while the \$1.5 million was the total of his buy/sell activity, "it is certainly not my profit."

However, the taxpayer's *pro forma* Schedule D and Form 8949 concede that the taxpayer received proceeds from the sale of cryptocurrency of over \$2 million, and his total trading volume reached over \$1.5 million. Also, the taxpayer did not submit any substantiation of the claimed basis in the cryptocurrency and other assets he acquired. Because the taxpayer failed to prove the amount of basis, the basis is deemed to be zero. Therefore, the taxable gain was the entire amount realized.



Filing and payment postponement traps to watch out for

Taxpayers affected by the Los Angeles County wildfires can avoid falling into these traps by being proactive.

By Renée Rodda, J.D.
Editor

For California taxpayers who were granted a Los Angeles County wildfire-related postponement of their filing and payment deadlines, the October 15, 2025, deadline is fast approaching. But there are a few traps that can catch practitioners and their clients by surprise.

Late K-1s are no excuse

Many California passthrough entities received the postponement to file their returns, including the K-1s, until October 15, 2025. This means many passthrough entity owners won't receive K-1s until October 15 or later.

The FTB and the California Office of Tax Appeals have consistently held that the late receipt of a K-1 is not reasonable cause for a late filing of a return and have refused to grant reasonable cause in these situations. But if the taxpayer can document the efforts they made to obtain the information and can demonstrate why they were unable to reasonably estimate their income from the entity, they may qualify for late-payment relief for any related underpayments.

Partners, shareholders, and LLC members should begin now to try to obtain information from the entity to timely prepare their return (and they should document these efforts). If they're unable to obtain the required information, they should make their "best guess" as to the passthrough income they'll receive and use that amount to timely file their own return. If their estimate is off, they can always file an amended return.

Confirm payments are made

As with late K-1s, taxpayers are expected to track whether any payments made via Web Pay are actually completed. If a taxpayer schedules a payment that ultimately doesn't go

through (for example, if two numbers in the account number are transposed), the taxpayer may not receive notice of the failed payment.

Taxpayers who are not aware that the payment never hit their account will not be granted reasonable cause for late-payment penalties. The FTB and the Office of Tax Appeals routinely hold taxpayers accountable for not exercising ordinary business care and prudence by checking whether money was withdrawn from their accounts when it comes to these types of transactions.

Avoid combining California estimates

When taxpayers are granted postponements for multiple estimated tax payments, many taxpayers make those payments as one single payment. Unfortunately, the FTB does not grant an automatic waiver to the mandatory e-pay requirement for these taxpayers. Because we're looking at up to four estimated tax payments being postponed until October 15, 2025, this will be an issue for even more taxpayers this year.

Remember that all payments made by an individual or corporation, regardless of taxable year or amount, must be remitted electronically to the FTB after the individual either has:

- Made a single estimated tax or extension payment greater than \$20,000; or
- Filed an original return with a tax liability greater than \$80,000.

If the total of the estimated tax payments made with one check or one e-payment is greater than \$20,000, your client will be required to make all future payments to the FTB electronically. For clients whose combined estimates will be in excess of \$20,000, we recommend splitting those payments into multiple payments below the threshold amount.

June 15 passthrough entity tax prepayment

Passthrough entities eligible to make the passthrough entity tax election were given until October 15, 2025, to make both:

- The 2024 final payment that was due by the original due date of the return (March 15, 2025, for calendar-year taxpayers); and
- The June 15, 2025, prepayment to qualify to make the election for the 2025 return.

Although the October 15 postponement provided relief for many taxpayers, it's important to avoid the following two potential traps:

1. Make sure the payments are made for the correct year. The 2024 remaining balance of the passthrough entity tax should be paid with the 2024 Form 3893, Pass-Through Entity Elective Tax Payment Voucher, and the June 15 prepayment for the 2025 tax year is paid with the 2025 Form 3893 voucher. If your clients are making payments with Web Pay, make sure they are crediting the payments for the correct year; and
2. Make sure your clients don't combine these payments with their payments for their other entity taxes that are due. The passthrough entity tax must be paid with either a Form 3893, on Web Pay, or via electronic funds withdrawal (EFW) using tax preparation software. They cannot be combined with the entity's other tax payments.

Both the prepayment of the tax and any other installment of the tax must be paid with Form 3893, on Web Pay or by EFW only. The entity cannot apply any other entity taxes that were overpaid to pay the passthrough entity tax. This means overpaid entity taxes cannot be applied to the June 15 prepayment.

Postponement Dates for Los Angeles County Fires

| Payment type | Due date (original) | Due date (disaster postponement) | FTB voucher | Separate payment required |
|--|-------------------------------------|----------------------------------|----------------------|---------------------------|
| 2024 Tax Year Payments Due October 15, 2025 | | | | |
| Personal Income Tax (PIT) Quarterly Estimated Tax Payments | 1/15/2025 | 10/15/2025 | 540-ES 541-ES | N* |
| PIT Payments | 4/15/2025 | 10/15/2025 | 3582 | N* |
| Business Entity (BE) Tax Payments | 3/15/2025 or 4/15/2025 | 10/15/2025 | 3586 3587 3588 | Y |
| Pass-Through Entity (PTE) Elective Payments | 3/15/2025 | 10/15/2025 | 3893 | Y |
| 2025 Tax Year Payments Due October 15, 2025 | | | | |
| PIT Quarterly Estimated Tax Payments | 4/15/2025 6/15/2025 9/15/2025 | 10/15/2025 | 540-ES 541-ES | N* |
| BE Quarterly Estimated Tax Payments | 4/15/2025 6/15/2025 9/15/2025 | 10/15/2025 | 100-ES | N* |
| Limited Liability Company (LLC) Annual Tax Payments | 4/15/2025 | 10/15/2025 | 3522 | Y |
| LLC Estimated Fee Payments | 6/15/2025 | 10/15/2025 | 3536 | Y |
| PTE Elective Tax Payments | 6/15/2025 | 10/15/2025 | 3893 | Y |
| * Note: PIT payments and PIT quarterly estimated tax payments that are for the same tax year can be paid as one payment | | | | |



Gambling on a residency audit was a losing bet

Taxpayers retained far too many connections to California after moving to Nevada.

By Sandy Weiner, J.D.
California Editor

A retired surgeon and nurse gambled big and lost big when they claimed they moved to Nevada but still spent a significant amount of time in California and retained significant California connections. The taxpayers claimed they moved to Nevada so the taxpayer husband could pursue his professional gambling career. However, the biggest gamble they took was claiming they were Nevada residents, and their loss cost them over \$6.5 million in additional taxes, penalties, and interest in the three tax years at issue. (*Appeal of Tran*, 2025-OTA-417)

The taxpayers were domiciled in Newport Beach, California, where they owned a home and their extended family resided. In late 2006 they purchased a condominium in

Henderson, Nevada, that was smaller than their California home. They never sold nor rented out the California home. They also retained their ownership interests in a California business and traveled back and forth to California numerous times per month for the taxpayer wife's medical treatments and to visit family and care for their aging parents.

The taxpayers argued that they became Nevada residents when they purchased their condominium, registered their cars, registered to vote, and also held interests in two other business entities registered in Nevada.

However, the OTA sided with the FTB in concluding that the taxpayers retained their California domicile and residency. The OTA noted that although taxpayers can have more than one residence, they can only be domiciled in one location.

Domicile

There was no question that the taxpayers were domiciled in California prior to purchasing their condominium in Nevada. The issue then was whether the taxpayers changed their domicile by taking up actual, physical residence in Nevada and whether they intended to remain in Nevada permanently or indefinitely. (R&TC §17014; *Whittell v. FTB* (1964) 231 Cal.App.2d 278, 284; *Noble v. FTB* (2004) 118 Cal.App.4th 560, 567-568)

The OTA found they did not. Their condominium in Nevada was smaller than their Newport Beach home. The residency timelines that the taxpayers presented and the Washington Mutual bank account statements did not demonstrate that the taxpayers spent more time in Nevada than California during any of the tax years at issue. Although the taxpayers contended that the days that were unaccounted for in their residency timeline were spent in Nevada, they failed to meet their burden of proof to substantiate their claims.

Even the taxpayer's stated intent to pursue his professional gambling career in Nevada was undermined when he testified that he often conducted his wagering online when he was in California. Therefore, the OTA found that the taxpayers did not abandon their California domicile.

Residency

Even though the taxpayers retained their California domicile, they could still be Nevada residents for tax purposes if they demonstrated that they were outside California for more than a temporary or transitory purpose. However, they failed to establish this. The OTA also found that they continued to maintain their closest connections to California during the tax years at issue by applying the following *Bragg* test criteria. (*Appeal of Bragg*, 2003-SBE-002)

Registrations and filings: Although the taxpayers registered their cars and obtained Nevada driver's licenses and had businesses registered in both states, the taxpayer husband did not register to vote in Nevada until October 2008, and therefore the OTA found that prior to that time, they maintained closer connection with California for purposes of the *Bragg* test registration and filings criteria.

Personal and professional associations: Both of the taxpayers' families were located in California as were the taxpayer wife's medical treatments. The evidence showed that the taxpayers returned to California anywhere from two days to two months at a time to visit family and attend medical appointments. Although the husband claimed he was pursuing his professional gambling career in Nevada, he did not join any Nevada associations and also testified that he conducted some of his gambling online while in California. Therefore, they continued closer connections to California under the personal and professional association criteria as well.

Physical presence and property: Because the taxpayers retained their larger home in California and spent more time in California, they also failed the physical presence and property criteria.



Renter's Credit to increase ... maybe

The increased credit will depend on annual budget allocation.

By Sandy Weiner, J.D.

California Editor

The Governor has signed AB 130 (Ch. 25-22), which provides for an increase in the Renter's Credit beginning with the 2026 taxable year, but only if there is an appropriation in the Budget Act for the taxable year to fund the increase. (R&TC §17053.5(a) and (k)) We will not know until next year's budget is passed if the credit will increase for the 2026 taxable year.

In tax years when there is a budget appropriation for the increased Renters' Credit, the credit available to qualified renters will be increased from \$120 (\$60 for single taxpayers or married taxpayers filing separate returns) to \$250 for all taxpayers without dependents.

If a taxpayer has a dependent, the credit is further increased to \$500.

Qualified renters

As before, the credit is only available to renters who are California residents and have an adjusted gross income of \$50,000 or less (\$25,000 or less if the taxpayer is single or is a married taxpayer filing separately).

In addition, the term "qualified renter" does not include:

- An individual who for more than 50% of the taxable year rented and occupied premises that were exempt from property taxes, unless possessory interest taxes or in-lieu tax was paid;
- An individual whose principal place of residence for more than 50% of the taxable year is with any other person who claimed such individual as a dependent for income tax purposes; or
- An individual who has been granted or whose spouse has been granted the Homeowners' Property Tax Exemption during the taxable year (this does not apply to an individual whose spouse has been granted the Homeowners' Exemption if each spouse maintained a separate residence for the entire taxable year).

Students

Students can claim the Renter's Credit, provided they meet all of the following requirements:

- The student must be a resident of California;
- Nonresident students who attend school in California do not qualify for the Renter's Credit;
- The student must have rented and occupied premises in California that constituted their principal place of residence during at least 50% of the taxable year. If someone other than the student (such as a parent) directly pays the rent, the student cannot claim the Renter's Credit;
- The premises cannot be exempt from property taxes. This means the student can't live in a dormitory (usually tax-exempt) and still qualify for the Renter's Credit. However, off-campus housing (such as an apartment) will probably qualify;
- When a person claims a student as a dependent, the student may not live with that person for more than half the year and qualify for the Renter's Credit. This means that if the student lives at home with their parents for more than 50% of the year and the parents claim the student as a dependent, the student will not qualify for the Renter's Credit. (R&TC §17053.5)

Military personnel

Military personnel cannot claim the Renter's Credit unless they are legal residents of California. However, a military spouse/RDP may claim this credit if they were a resident, did not live in military housing during the tax year at issue, and are otherwise qualified.

Mobile homes

Mobile homes, even if owned by the taxpayer, located on rented or leased land, can qualify for the Renter's Credit if the county assessor has not granted the Homeowners' Exemption for the mobile home. (R&TC §17053.5(h))

Limitations and carryover

The credit may reduce regular tax below tentative minimum tax. (R&TC §17039) The credit is nonrefundable and may not be carried over.

Form

The credit is claimed directly on FTB Form 540, line 46.



Reporting IRS changes to the FTB

Taxpayers need to report the change in a timely and detailed manner.

By Kathryn Zdan, EA
Contributing Editor

When the IRS changes or corrects a taxpayer's federal tax return, within six months of the IRS's final determination the taxpayer is required to report the change to California, either conceding to the change or stating that the IRS's determination is erroneous. (R&TC §18622) If the FTB makes a deficiency assessment based on the federal adjustment, that assessment is presumed to be correct. The taxpayer must provide credible evidence that the FTB's assessment is not correct; otherwise, the FTB's assessment will be upheld.

In a recent appeal, the IRS adjusted taxpayers' gross income to account for unreported securities income, and the FTB made corresponding adjustments based on information received from the IRS. (*Appeal of Elliston*, 2025-OTA-418) The taxpayers argued that the securities were inherited, and they were entitled to additional basis and claimed that the IRS had changed its determination. However, they did not provide any evidence that the IRS had canceled or reduced the federal assessment, and without support, the FTB's assessment was upheld.

Final federal determination

The date of the final federal determination is the date on which each adjustment or resolution resulting from an IRS examination is assessed pursuant to IRC §6203 (referred to as the 23C date), not when the issue is resolved by a court. (R&TC §18622(d))

Taxpayers can identify the 23C date by referring to the IRS assessment, overpayment, or no-change notice once the adjustment is assessed. The FTB can identify the 23C date by checking for corresponding entries in the IRS Master File.

Extended limitations period

A special statute of limitations period applies if the California deficiency arises from adjustments made to the federal return. (R&TC §§18622, 19059, 19060) If the FTB receives notification of a federal change from either the taxpayer or the IRS:

- Within six months of the final federal determination, the FTB has two years from the notification date to issue an assessment;
- After the six-month period following the final federal determination, the FTB has four years from the notification date to issue an assessment; or
- If neither the IRS nor the taxpayer notify the FTB of the final federal determination, there is no statute of limitations, and the FTB can issue an assessment at any time.

Notice must be detailed

Under R&TC §18622, the notification must be “sufficiently detailed” to enable the FTB to compute the resulting California tax liability, or the statute of limitations period will remain open. The statute does not define “sufficient,” but FTB Publication 1008, Federal Tax Adjustments and Your Notification Responsibilities to California, states that you must:

- Tell the FTB a federal adjustment has been made;
- Identify the years that were adjusted;
- Fully explain all adjustments; or
- Provide federal documentation showing the adjustments made to taxable income.

(Appeal of Valenti, 2021-OTA-093P)

FTB Publication 1008 also states that you “should” (indicating that these items are not mandatory) provide the FTB with:

- A complete copy of all final federal determinations (IRS revenue agent reports (RARs), settlements, Tax Court decisions, closing agreements), including all schedules;
- Copies of original and revised schedules and forms, noting state and federal differences;
- A complete copy of the state and federal tax returns for a final federal determination that affects a taxable year more than three years older than the current year; and
- A telephone number where the taxpayer can be reached should the FTB have any questions (be sure to attach Form FTB 3520, Power of Attorney Declaration, if the FTB will be contacting the taxpayer’s representative).

The FTB and the OTA are quite insistent that the notice provided not only alert the FTB that adjustments were made but show the actual adjustments made by the IRS, the exact amounts involved, and the computations so that the FTB is able to compute the resulting change to the taxpayer’s California’s tax. A taxpayer’s failure to do so resulted in the OTA applying an extended statute of limitations, even though the taxpayer provided copious documentation regarding the IRS’s assessments, including a letter from the taxpayer that attached Tax Court petitions, and decisions and closing agreements entered into with the IRS. *(Appeal of Thompson, 2024-OTA-065)*

Request date of notification

If a taxpayer receives a Notice of Proposed Assessment from the FTB based on a federal revenue agent report, the taxpayer can request the date of notification from the FTB by calling the FTB at:

(800) 852-5711

Practitioners can get the same information by calling the Tax Practitioner Hotline at:

(916) 845-7057



Correction

In the May 2025 issue of *Spidell's California Taxletter*® in the article "Understanding California's excess business loss limitation" we stated that California does not conform to the CARES Act change that states that excess business loss "shall be determined without regard to any deductions, gross income, or gains attributable to any trade or business of performing services as an employee." As a result of this nonconformity we concluded that wages are treated as income from a trade or business that could offset nonwage business losses.

The FTB has reached out to clarify that although California does not conform to this CARES Act technical amendment, California does conform to IRC §62(a)(1), which states:

IRC Sec. 62(a) For purposes of this subtitle, the term "adjusted gross income" means, in the case of an individual, gross income minus the following deductions:

(a)(1) The deductions allowed by this chapter (other than by part VII of this subchapter) which are attributable to a trade or business carried on by the taxpayer, if such trade or business does not consist of the performance of services by the taxpayer as an employee.

The FTB is taking the position that because this CARES Act technical amendment is consistent with IRC §62(a)(1), they are still excluding wage income earned as an employee from the trade or business income used to compute the excess business loss limitation. Therefore, no adjustment is allowed for wage income when determining the trade or business income used to compute the California excess business loss.

The FTB is looking into revising the FTB Form 3461, California Limitation on Business Losses, to avoid any future confusion.

We have updated the May 2025 article online as follows and will provide further clarification in an upcoming issue of the California Taxletter:

Nonconformity issues

California also modifies the federal excess business loss limitation to require that the excess business loss calculation be applied after applying California's passive loss provision (which ignores real estate professional status and makes modifications for California credits) rather than the federal loss provision. (IRC §461(l)(6)) Therefore, losses suspended in the current tax year under the passive loss rules do not have an effect in the current year. Any prior-year suspended losses that are released in the current year do have an effect in the current year.

California does not conform to the CARES Act amendments that:

- Exclude NOLs, IRC §199A, and capital loss deductions from the business deductions used to calculate the excess business loss;
- Exclude wages from the excess business loss computation; and
- Limit the capital gains included in the excess business loss computation to the lesser of:
 - Capital gain net income solely attributable to gains and losses from a trade or business; or
 - The taxpayer's capital gain net income.

Wages and the excess business loss calculation

As stated above, California does not conform to the CARES Act change to the federal excess business loss provision that excludes wages from the business income calculation. (IRC §461(l)(3)(B)(ii)) Specifically, the CARES Act provision states that the excess business loss "shall be determined without regard to any deductions, gross income, or gains attributable to any trade or business of performing services as an employee."

On Form FTB 3461, California Limitation on Business Losses, taxpayers must include wages, salaries, tips, etc., and unemployment compensation in their calculation of income attributable to a trade or business.

Because wage income is considered part of the taxpayer's trade or business income on Form FTB 3461, the wage income offsets the amount of nonwage business losses, which will allow a taxpayer to deduct a greater portion of their current-year losses:

Example of federal/California wage treatment difference: In 2025, Jenny has \$400,000 in business losses and \$300,000 in W-2 income. She has no other income or losses. Wages are not classified as business income for federal purposes, so Jenny will have more of her nonwage business losses limited in the current year, leaving a larger federal carryover compared to California:

The following calculation summarizes the different federal and California wage treatment:

| | Federal | California |
|---|-------------|-------------|
| Nonwage business losses | (\$400,000) | (\$400,000) |
| Wages (treated as business income for CA, not federal) | N/A | 300,000 |
| Overall business loss for purposes of calculation | (\$400,000) | (\$100,000) |
| Lesser of limitation amount or overall business loss | 313,000 | 100,000* |
| Loss carryover to the following year | (\$ 87,000) | \$ 0 |
| * California's excess business loss limitation is the same as the federal amount of \$313,000, but because Jenny's overall business loss is only \$100,000, she does not have any excess business losses in the current year. | | |

The difference in the California and federal losses will be reflected on Schedule CA (540), Part I, Section B, line 3.



THUMB TAX

CDTFA issues proposed amendments to technology transfer agreement regulations — The CDTFA has released a discussion paper that outlines proposed amendments to 18 Cal. Code Regs. §§1502 and 1507 to clarify the application of tax to transactions involving the sale and use of software, consistent with caselaw. (See *Nortel Networks, Inc. v. State Board of Equalization* (2011) 191 Cal.App.4th 1295; *Lucent Technologies, Inc. v. State Board of Equalization* (2015) 241 Cal.App.4th 19) The CDTFA also proposes new regulation §1507.1, which would clarify the taxation of software transactions and “establish presumptions to help taxpayers and the Department determine whether there is a software TTA, and the value of hardware transferred under a software TTA.”

This discussion paper is available at:

<https://cdtfa.ca.gov/taxes-and-fees/TTADP071025-Accessible.pdf>

We will provide updates following the July 24, 2025, interested parties meeting regarding these regulations.

CDTFA announces new office location — On July 7, 2025, the CDTFA opened its new Santa Ana office for in-person assistance. (CDTFA Updates (July 16, 2025)) The office is located at 1 MacArthur Place, Suite 400, Santa Ana, CA 92707-7704. The CDTFA's in-person assistance offices are open Monday through Friday from 8:00 a.m. to 5:00 p.m.

2025 BOE Taxpayers' Bill of Rights Hearing — The Board of Equalization has announced the 2025 Taxpayers' Bill of Rights Hearing, which will be held on August 20, 2025, at the May Lee State Office in Sacramento. (BOE LTA No. 2025/016, available at: www.boe.ca.gov/proptaxes/pdf/lta25016.pdf) The public hearing provides taxpayers, county assessors, and other local agencies the opportunity to provide comments on items discussed in the BOE's Taxpayers' Rights Advocate Fiscal Year 2023-24 Annual Report. Additionally, parties have the opportunity to comment on all BOE-administered programs and local property tax matters.

Parties may attend this hearing in person, submit comments in writing, or call into the meeting. Anyone interested in being scheduled as a speaker at the hearing or submitting comments for the hearing should refer to information on the BOE website at:

www.boe.ca.gov/tra/

Contact the BOE's Taxpayers' Rights Advocate with questions at:

(916) 274-3400

Erroneous refund check does not negate perfected claim for refund — In a pending precedential decision, the OTA had jurisdiction to hear an appeal from taxpayers who, at the time of appeal, had not repaid the FTB an erroneously refunded amount. (*Appeal of Leebow*, 2025-OTA-426P) The FTB refunded the taxpayers \$42,898 but later sent them a notice stating that the refund was in error and that the taxpayers were required to repay \$23,515. Because as of the date of the appeal hearing the taxpayers had not yet repaid this amount, the FTB argued that the taxpayers' claim had not been perfected and therefore the OTA did not have jurisdiction to hear the appeal.

However, the OTA noted that the taxpayer's original claim was already perfected because they had already fully paid taxes, penalties, and interest due. The FTB's subsequent issuance of an erroneous refund check does not retroactively negate the fact that the taxpayers filed a perfected claim for refund which was denied by the FTB.

Regarding the underlying issue of the penalties, the OTA disagreed with the taxpayers' arguments regarding reasonable cause for abating the estimated tax and late-payment penalties; the taxpayers argued for penalty abatement due to the COVID-19 pandemic and fluctuating income that made it difficult to calculate and pay their tax liability.

Postponed filing date does not affect statute of limitations deadline — In a pending precedential decision, a taxpayer's untimely filed claim for refund was disallowed because a state of emergency postponement did not extend the four-year statute of limitations. (*Appeal of Nguyen*, 2025-OTA-333P)

The taxpayer filed her 2019 return on May 9, 2024. She argued that the four-year statute of limitations for filing a claim for refund was extended by the COVID-19 emergency postponement that extended the filing and payment deadline for 2019 returns to July 15, 2020; under her reasoning, the four year-statute of limitations expired on July 15, 2024, and her claim for refund was timely. However, the postponement of the due date does not change the four-year statute of limitations date, which is based on the original filing deadline of the return, April 15, 2019. (R&TC §§18572(b), 19036(a))

Editorial Staff



Editor
Renée Rodda, J.D.



California Editor
Sandy Weiner, J.D.

Contributing Editor
Kathryn Zdan, EA
Mike Giangrande, J.D., LL.M.

Managing Editor
Austin Lewis

Layout
Ana Cervantes

OTA rejects California filing status change — A taxpayer was denied a refund claim where she filed an amended California return that changed her filing status only for state purposes. (*Appeal of Alvillar*, 2025-OTA-415) The taxpayer originally filed her 2018 California return as single with federal AGI of \$141,592 and received a \$5,570 refund. The IRS audited her federal return and increased her AGI to \$196,192 due to unreported pension income. After the FTB issued its assessment, the taxpayer filed an amended California return using head of household status and claiming a \$3,262 refund. However, a taxpayer is required to use the same filing status for federal and state purposes. (R&TC §18521) Note that for married filing separate taxpayers, there are limited exceptions to this rule.

The taxpayer argued that the IRS “approved” her use of HOH status, but the FTB found no evidence that she had filed an amended federal return. The OTA noted that even if the IRS had accepted the amended return and filing status, the FTB is not bound to accept a filing status if it believes it is erroneous. (R&TC §17042)

New feature allows additional representatives to be added to OTA appeals — A new feature is now available on the Office of Tax Appeals portal. The feature allows representatives to add up to two additional representatives to new or existing appeals. The additional representatives will receive full access to the appeal and all automated e-mail communication.

A step-by-step video on adding additional representatives to a new appeal is available at:

<https://youtu.be/iFwINeEA5qg>

A step-by-step video on adding additional representatives to an existing appeal is forthcoming.

CALIFORNIA CONTACTS

| | |
|--|--|
| The FTB maintains a list of all notices with information on how to respond at: | www.ftb.ca.gov/help/letters/index.html |
| Los Angeles County wildfire victims can contact the FTB if the taxpayer received an erroneous notice at: | FTBLACountyDisasterRelief@ftb.ca.gov (888) 825-9868 www.ftb.ca.gov/myftb/index.asp |
| If a taxpayer receives a Notice of Proposed Assessment from the FTB, contact the FTB to request the date of notification at: | Taxpayer: (800) 852-5711 Tax Practitioner Hotline: (916) 845-7057 |
| To see the CDTFAs discussion paper that outlines proposed amendments to 18 Cal. Code Regs. §§1502 and 1507, go to: | https://cdtfa.ca.gov/taxes-and-fees/TTADP071025-Accessible.pdf |
| To see more information about submitting comments at the 2025 Taxpayers’ Bill of Rights Hearing, go to or call: | www.boe.ca.gov/tra/ Taxpayer’s Rights Advocate Office: (916) 274-3400 |
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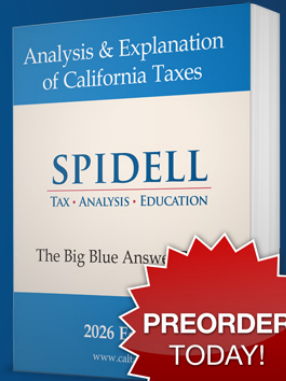
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