

Supplement CA

California Tax Forms Guide 2005 Edition

The Basics
Changes You Should Note
Installation and Start-up
Translating the Federal Return
Printouts for the FTB
Form by Form Details

This document is not a stand-alone manual. It is a special supplement to the User's Guide for HowardSoft's Tax Preparer and the Tax Forms Guide for the 2005 Edition of HowardSoft's Form 1040 software, and relies on those guides as the main source of instructions for the California Supplement software. This document and the associated software are based on information compiled and interpreted by HowardSoft late in 2004 and January 2005, including the latest information from the FTB, but their complete accuracy cannot be guaranteed. Neither HowardSoft nor Dr. J. E. Howard assumes any responsibility for any consequential damages resulting from their use.

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The Basics

What it is. The *California Supplement 2005* is a special supplement to the regular 2005 Edition of *Tax Preparer®*. It adds to the regular edition (for preparing Form 1040 returns), the ability to prepare California FTB Form 540 returns. It uses data from the computer-prepared federal (Form 1040) return as the starting point for the California return through its built-in “translate” feature, resulting in the computer-automated preparation and printing of state tax returns for the same tax year. The state forms that are built-in are comparable to the federal forms in the regular edition, as seen in Table CA-1.

This document supplements the Tax Forms Guide 2005 Edition. This document adds to the Tax Forms Guide instructions for California forms. However, where calculations and instructions are the same as the comparable federal forms, *this document refers to the regular Tax Forms Guide*.

CAUTION: You MUST Prepare the federal return FIRST. To use the California Supplement you must prepare the federal return *first*. Once the federal return is complete and final calculations for it have been performed, the California Supplement can translate the federal data into a California return. You do not need to enter any data manually except where California law requires different entries from those that appear on the federal return.

Not intended for nonresidents nor fiscal filers. California law is especially different from federal law for nonresidents and part-year residents of California. *CAUTION: You, and spouse if filing jointly, must have been a resident of California for the entire year to use Form 540, for which this software is specifically designed.* If either you or spouse was a nonresident *AT ANYTIME* during the tax year, you must file Form 540NR instead of Form 540. Although this software will provide the necessary calculations for most supporting forms and schedules, it does not provide Form 540NR, which is unique in its prorationing of incomes and tax among states. In addition, individuals who use a tax year other than a calendar year cannot use this software because it does not provide the necessary prorationing among years. See the official FTB instructions for more details.

Table CA-1. Forms Provided in California Supplement

| CALIFORNIA FORM/SCHED | TITLE OF CALIFORNIA FORM/SCHEDULE | FEDERAL EQUIVALENT |
|-----------------------|---|--------------------|
| Control | Automation Control Form | Control |
| Form 540 | California Long Form | Form 1040 |
| Schedule CA | California Adjustments | Form 1040 |
| Schedule D | Capital Gain or Loss Adjustment | Schedule D |
| Schedule D-1 | Sales of Business Property | Form 4797 |
| *Schedule G-1 | Tax on Lump Sum Distributions | Form 4972 |
| Sch. P, pg 1 | Alternative Minimum Tax | Form 6251 |
| Sch. P, pg 2 | Credit Limitations | None |
| Schedule S | Other State Tax Credit | None |
| *Form 3501 | Employer Child Care Pgm/Contribn Credit | None |
| *Form 3504 | Long-Term Care Credit | None |
| Form 3505 | Teacher Retention Credit | None |
| Form 3506 | Child & Dependent Care Expenses Credit | Form 2441 |
| *Form 3508 | Solar Energy System Credit | None |
| *Form 3510 | Credit for Prior Year AMT | Form 8801 |
| Form 3519 | Payment Voucher for Automatic Extension | Form 4868 |
| *Form 3521 | Low-Income Housing Credit | Form 8586 |
| *Form 3523 | Research Credit | Form 6765 |
| *Form 3526 | Investment Interest Expense Deduction | Form 4952 |
| *Form 3533 | Change of Address | Form 8822 |
| *Form 3535 | Manufacturers' Investment Credit | None |
| Form 3540 | Credit Carryover Summary | None |
| *Form 3548 | Disabled Access Credit | Form 8826 |
| *Form 3553 | Enterprise Zone Employee Credit | None |
| Form 3800 | Tax for Children with Investment Income | Form 8615 |
| Form 3801 | Passive Activity Loss Limitations | Form 8582 |
| *Form 3801-CR | Passive Activity Credit Limitations | Form 8582-CR |
| Form 3803 | Election for Child's Interest/Dividends | Form 8814 |
| Form 3805E | Installment Sale Income | Form 6252 |
| Form 3805P | Add'l Tax on Qlfd Plans (IRAs, etc) | Form 5329 |
| *Form 3805V | NOL Comp'n/NOL & Disaster Loss Limits | Form 3621 |
| *Form 3805Z | Enterprise Zone Deductn & Credit Summary | None |
| *Form 3806 | LARZ Deduction and Credit Summary | None |
| Form 3885A | Depreciation & Amortization Adjustments | Form 4562 |
| *Form 5123 | Employer-Provided Adoption Assistance Exclusion | Form 8839 |
| Form 5805 | Underpayment of Estimated Tax | Form 2210 |
| & 5805-F | Underpayment by Farmers and Fishermen | & 2210-F |
| Form 5805 | Pt III, Annualized Installment Schedule | 2210, SchAI |
| *Form 5870A | Tax on Accumulation Distribn of Trusts | Form 4970 |
| Worksheet A | Itemized Deductions | Schedule A |
| Worksheet B | Interest and Dividends | Schedule B |
| Worksheet C | Business Income | Schedule C |
| Worksheet E | Supplemental Income | Schedule E |
| Worksheet F | Farm Income | Schedule F |
| worksht 4835 | Farm Rental Income | Form 4835 |
| Form 540-ES | Estimated Tax Worksheet | Fm 1040-ES |
| Form 540X | Amended Individual Income Tax Return | Form 1040X |
| **Form 8453 | Income Tax Declaration for e-file | Form 8453 |
| **Form 8454 | e-file Opt-Out Record | None |

Forms not built into the software are available from the FTB through a link on our web page at www.howardsoft.com.

*Included in Premium Level program only. Instructions for these forms appears in a separate Premium Level Supplement.

**Included in Standard and Premium Level programs only.

FTB tightens printing rules for paper returns: NO MORE TEXT-MODE FACSIMILES! At the end of 1997, the FTB banned all use of non-graphic forms for tax returns, *including all supporting schedules and forms*. This means that you now have only the following options for filing:

1. Computer-printed graphics using HowardSoft's Standard or Premium Level California Supplement.
2. Computer-printed data on plain paper, photocopied using transparent overlays sold by HowardSoft for this purpose.
3. Computer-printed data on a preprinted scannable Form 540 form sold by HowardSoft, plus 1 or 2 for all other forms and schedules.
4. Manually-prepared forms using only the FTB official forms with their large boxes for manual entry of name and SSN at the top of each form, and bar-codes in the lower-left corner of each page.
5. Electronic filing using HowardSoft's Electronic Filing Option for California returns.

The current FTB rules are a consequence of the large investment the FTB has made in automated equipment that relies on graphic lines and symbols, neither of which can be reproduced by text-mode dot-matrix printers. Moreover, the FTB recommends the use of laser printers or high-quality ink-jet printers for computer-generated forms, so that its automated equipment can quickly align the form. While it may seem that this only results in more money for the software vendors like HowardSoft, *we are strongly opposed to the change because it creates a hardship for professionals with a small tax practice or individuals who have little time for manual transferring of numbers onto FTB forms*. But we must abide by the FTB rules in order for our print-outs to be approved by the FTB.

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Changes You Should Note

Changes You Should Note

Several taxes and credits indexed with inflation. The indexing for 2004 returns is 3.1% relative to 2003 returns. As a result, several calculations have changed, including:

Standard deductions increased from \$3,070 to \$3,165 for taxpayers filing single or married filing separately, and from \$6,140 to \$6,330 for all others.

Personal exemptions increased from \$82 to \$85 for each exemption.

Dependent exemptions increased from \$257 to \$265 for each exemption.

Thresholds for phaseout of exemptions and itemized deductions increased to \$139,921 for single and married filing separately, \$209,885 for head of household, and \$279,846 for married filing jointly and qualifying widow(er). The former thresholds were \$135,714, \$203,574, and \$271,432, respectively.

Ceiling for joint custody head of household credit and dependent parent credit increased from \$327 to \$337. The credit remains at 30% of net tax.

Ceiling for qualified senior head of household credit increased from \$1,000 to \$1,031, and the AGI to which it applies increased from \$53,084 to \$54,730. The credit remains at 2% of taxable income.

Tax brackets indexed with inflation. The tax brackets for the tax rate schedules, upon which the tax tables are based, have been indexed with inflation as well. The old and new rates are compared in Table CA-2.

Table CA-2. Tax Rate Schedules

| TAX RATE | TAXABLE INCOME ABOVE WHICH TAX RATE STARTS | single & mfs | mfj & qw | h of h |
|--------------------|--|--------------|----------|--------|
| FOR TAX YEAR 2003: | | | | |
| 1.0% | \$ | 0 | 0 | 0 |
| 2.0% | | 5,962 | 11,924 | 11,930 |
| 4.0% | | 14,133 | 28,266 | 28,267 |
| 6.0% | | 22,306 | 44,612 | 36,437 |
| 8.0% | | 30,965 | 61,930 | 45,096 |
| 9.3% | | 39,133 | 78,266 | 53,267 |
| FOR TAX YEAR 2004: | | | | |
| 1.0% | \$ | 0 | 0 | 0 |
| 2.0% | | 6,147 | 12,294 | 12,300 |
| 4.0% | | 14,571 | 29,142 | 29,143 |
| 6.0% | | 22,997 | 45,994 | 37,567 |
| 8.0% | | 31,925 | 63,850 | 46,494 |
| 9.3% | | 40,346 | 80,692 | 54,918 |

AGI ceiling for Renter's Credit raised. For tax year 2004, no Renter's Credit is allowed if California AGI exceeds \$59,910 for married taxpayers (\$29,955 for single and married filing separately). These figures are up from \$58,108 and \$29,054 for 2003. Full credit is allowed below these amounts; there is no gradual phaseout.

Teachers Retention Credit (Form 3505) suspended for 2004 and 2005. This credit was suspended for tax year 2002, was reinstated for 2003, but is now suspended again for tax years 2004 and 2005. (When not suspended the law provides a credit up to \$1,500 for qualifying credentialed teachers of grades kindergarten through 12th grade.)

Two new California funds for voluntary contributions. California has long made it easy taxpayers to make contributions to certain charities through their Form 540 tax return. This year two more funds appear on the form. The *California Military Family Relief Fund* is used to aid members of the California National Guard who have been called to active duty. The *California Prostrate Cancer Research Fund* is used to fund research on prostrate cancer.

California has NOT conformed to the federal special first-year 30% or 50% special depreciation allowance, nor the increase in section 179 ceiling to \$100,000 in 2003 (indexed with inflation thereafter). California has a good record in recent years of bringing California law into conformance with federal law to simplify the preparation of a California return. However, recent Federal tax acts have been too extreme for California. *There will therefore now be a big difference between federal and California depreciation deductions for most tangible property placed in service after September 10, 2001.*

Installation and Start-up

Use User's Guide for installation instructions. The installation and start-up in the introductions of the separate User's Guide apply to this California Supplement as well. *The standard installation puts all edition years and all supplements in the same hard disk subdirectory C:\TAX*, and all programs for the same tax year share the same custom settings, program settings, and start-up programs. With this standard installation, you are greeted upon start-up by a menu that gives you a choice of which version or edition to start. The California Supplement 2005 adds the California supplement as a choice for the 2005 Edition year. For example, if you have the current-year regular edition and California Supplement installed in the same subdirectory, you are given the choices

1 Federal (Form 1040 returns)

2 California (Form 540 returns)

You must press 2 (or mouse-click onto choice 2) to select the California Supplement. (If you make no choice after a short pause, the software will choose the federal 1040 version for you.) After you make your choice the selected version is started and soon appears on the screen.

Apple only:

Hint for Apple II computers with 3-1/2" drives. If your working copy of the program for the Federal Edition is a 3-1/2" disk, you can usually install the California Supplement on the same disk. To do so, you should treat the federal disk like a hard disk and install the California program onto it. Start the California program as you normally would, but press U (for Utilities) as soon as the ProDOS screen disappears. You are then greeted with a menu of three choices, second of which is

2. INSTALL CAL ON HARD DISK

When you make this choice you are led through the installation, and required to specify the name of the hard disk. If installing directly on the HowardSoft-supplied 3-1/2" Program Disk for the Federal Edition, you should enter /TP98IUS for the hard disk. Otherwise you should enter the name you gave your working copy of the disk when you created it. The necessary California files are then copied to the Federal disk.

Add a California tax directory first. Since California Supplement contains no pre-stored data, you must add a tax directory to the Storage Disk the first time you use the California Supplement for the new tax year. If you don't remember how, refer to Chapter 9 of the separate User's Guide. The tax directory you create by this process is completely independent of any tax directory created with any other edition of any other type or year.

Translating the Federal Return

Translation is the key to a successful return. Because the California return uses numerous results from your federal return, it is essential to start a California return ONLY after the federal return is complete and fully calculated. You should use the built-in “translate” feature, which will copy all relevant information from the federal return into a state file (which will remain separate from the federal return thereafter).

Preview of the process. Federal returns are used to generate California returns through a 3-step process:

- 1 Translation.** A copy of the federal file is generated in the California format, ready for use with the California Supplement.
- 2 Adjustment.** Any federal data that needs to be altered for the California return, or new data that have to be added, are entered next using supporting forms and worksheets when available.
- 3 Calculation.** The entire return is finally recalculated from beginning to end using the California state tax laws.

The return is then ready to be printed, signed, and filed with the FTB.

Translation: Let Chapter 9 of User's Guide be your guide. Once your hard disk or separate Storage Disk has a California tax directory on it, you can proceed with the translation using the instructions at the end of Chapter 9 of the separate User's Guide, with the following exceptions:

- A** Where those instructions call for a Prior-Year Storage Disk, interpret it as the Current-Year Federal Storage Disk.
- B** Where those instructions call for a Current-Yr Storage Disk, interpret it as the Current-Year California Storage Disk (to which you must add a California tax directory to hold the translated return).
- C** When asked if you want to “Transfer all prior \$ amounts?” you MUST answer YES to produce a valid California return from the federal data. (Unlike translation from prior-year returns, the translation from federal returns to California returns almost always uses the original federal numbers without modification.)
- D** When asked if you want to “Transfer supp'g statements?” you should answer Yes so that the California return will have all the detailed support that is relevant to it. A Yes answer is mandatory for returns with passive activity losses because the supporting worksheets contain details required for the proper interaction with California Form 3801 (the equivalent of federal Form 8582).

Adjustment: Enter differences from federal entries. Because California law now closely parallels federal law, it is often possible to produce a valid California return with little or no adjustment to the entries from the translated federal return. (We recommend FTB Publication 1001, *Supplemental Guidelines to California Adjustments*, to help you determine where adjustments may be necessary. This and other FTB publications cited in this document are available for free downloading from the FTB through a link on our web page at www.howardsoft.com.) Nevertheless, you should view all translated

Translating the Federal Return

worksheets to ensure that they are calculated under California laws. If you are depreciating ANY assets placed in service before 1987, you will likely need to make adjustments because of prior differences between federal and state law. You must access every worksheet translated to California Form 3885A to let the computer know the depreciation methods and basis to use for nearly all assets. While California has conformed in many areas of depreciation and section 179 expense in recent years, it has NOT conformed with the federal 30% and 50% bonus depreciation (named the "special allowance" by the IRS), which is a required first-year depreciation allowance for most property unless you elect out of it. Furthermore, California has never conformed to federal rules for Indian Reservation Property or depreciation for nonresidential rentals, and now differs markedly in its limitations on Sec. 179 expense. You will therefore have to make adjustments on worksheets for the appropriate copy of Form 3885A if any of these situations apply to you. You may also have to view every W-2 Worksheet in order to remove any non-SDI amounts translated to the SDI line (since the entire amount labeled "Other non-fed tax" on the federal W-2 Worksheet is translated to "SDI tax withheld" on the California W-2 Worksheet) and to ensure that any excess SDI tax collected (for having more than one employer) is properly computed. If you have to make a large number of adjustments, you may find it helpful to print prior-data *pro forma* sheets for the translated files, as described in Chapter 11 (page 11-4) of the separate User's Guide. Pro forma sheets show the translated data with blank lines alongside for noting changes.

Additional changes may be needed for scannable Form 540. The format for the address block of Form 540 is especially constrained on a scannable Form 540. You must generally use the same rules of abbreviation for entering your name and address as the FTB-provided address labels. In addition, if one of the taxpayers is deceased, you must supply the date deceased, and the executor's name if there is no surviving spouse. The software provides additional entries for these additional items, as detailed later.

Calculation. Calculations for the return must be completed before you can produce an official printout. REMINDER: No recalculation is involved in the Translation Phase. You must cause recalculation yourself either by entering the return and allowing it to recalculate when you exit, by pressing the Recalculate Key (Shift-F8 or ctrl-B), or by choosing the Recalculate option from the Prepare Returns Menu (Figure 10-1 in Chapter 10 of the User's Guide).

CAUTION: If you amend the federal return, you must amend the California return. Once you have copied all federal data into a California data file by means of "translation," you must remember that the California return is now based on that federal data. The translation ensures that the California return is consistent with the federal return automatically. However, if you change any entries on the federal return AFTER you have translated it into a California return, you will have to make a corresponding change in the California return manually yourself to ensure that the two are still consistent.

Printouts for the FTB

Strict requirements for FTB printouts. Official printouts for the FTB can be generated once the final calculations are complete. However, FTB requirements for printouts are much stricter than IRS requirements. In summary, Form 540 returns must follow these rules:

Form 540. The FTB now requires a scannable Form 540 designed for preparation by tax software like ours. A conventional Form 540 is no longer acceptable for a computer-prepared Form 540. A computer-prepared Form 540 must be generated in the scannable Form 540 format using only a laser, ink-jet, or other high-quality printer. This format is automatically provided by the software when you use our Standard of Premium Level software, for which the graphics of the scannable Form 540 are built-in. Although the software can also print a facsimile Form 540 in the conventional Form 540 format, it cannot be filed with the FTB. If you cannot meet the printing requirements for a scannable Form 540, as highlighted on the next page, you must file a manually-prepared conventional Form 540 as printed and distributed by the FTB. (The software provides a fill-in mode to aid you in this effort when you choose NO for "Bypass alignment dots.") *CAUTION: Additional care is required in your entries for taxpayer information when you use the scannable Form 540 because the printed format must follow strict guidelines like those that the FTB uses when it generates mailing labels for taxpayers. You must also follow the special rules detailed later when you assemble the return for filing.*

Forms 3519, 3582 (e-file only), and 540-ES. The FTB also now requires that all computer-prepared payment vouchers be scannable vouchers. These vouchers include a scannable area with taxpayer information in the same format as the scannable Form 540 plus an OCR line that summarized the taxpayer and the amount of payment. The vouchers printed by this software using the Laser-graphic or Windows-graphic capabilities that are built into our Premium Level software satisfy this requirement. If you cannot print by these methods you must send hand-prepared vouchers instead.

Form 540-X. While it doesn't have a complete scanband like Form 540, a computer-prepared Form 540-X must now use the scannable 540 format for taxpayer information at the top of page 1 of the form. The form printed by this software using the Laser-graphic or Windows-graphic capabilities that are built into our Premium Level software satisfy this requirement. If you cannot print by these methods you must file a hand-prepared Form 540-X.

All other forms and schedules. While the other forms and schedules do not have a scannable data area like the scannable Form 540, they still must be FTB-approved graphic forms. All FTB forms and schedules now have a special registration marks and a document ID that identifies the software that prints the form. The FTB now re-

quires that all computer-generated forms be generated with high-quality graphics on a laser or high-quality ink-jet printer. Text-mode facsimiles are no longer acceptable, and our facsimile printouts now carry the slogan DO NOT FILE THIS FORM, as required by the FTB. (We still produce facsimile forms that duplicate the layout of the FTB graphic forms, which you can use for your or your clients' files, but the FTB will no longer accept them for filing.)

Federal return. California has in recent years required that a copy of the complete federal Form 1040 and its schedules be submitted with the California return whenever you file Form 540. However, you do not have to attach the federal forms if you had to file no more than Schedules A and B with the federal return. *SPECIAL RULE: If the filing status on the California return is different from that on the federal return, you will have to recompute the federal AGI based on the California filing status and data. You must then file with your Form 540 return BOTH the official Form 1040 you filed with the IRS and this recomputed Form 1040.*

Scannable Form 540 required for computer-generated returns. Thanks to the automated equipment that the Franchise Tax Board (FTB) now uses for processing returns, the requirements for printouts you file with the FTB are quite different than they were just a few years ago. There are now only two ways to file Form 540:

1. Computer-prepared Scannable Form 540 using HowardSoft's Laser-graphic or Windows-graphic capabilities, or overlay forms.
2. Manually-prepared official Form 540 as printed and distributed by the FTB.

The scannable Form 540 includes a special scan patch that calibrates the automated equipment, and a scan band area where summary data is printed by the computer. If you use a computer to print the form, it must be the scannable Form 540. Conversely, if you do not use a computer to print the form, you cannot use the scannable Form 540. This California Supplement fully supports the FTB form, whether you use pre-printed forms, overlays, or Laser-graphic or Windows-graphic capabilities for printing the official return that you file with the FTB. Whenever you choose to produce a fill-in Form 540, the printout is designed for the scannable Form 540 as long as your program settings show "Yes" for "Bypass alignment dots." But there are additional requirements imposed by the FTB:

1. Printer must be laser, ink jet, daisy wheel, or letter-quality dot-matrix.
2. Entries must be printed in upper case using standard pica Courier typeface (10 characters per inch across and 6 lines per inch down). (Upper casing is automatic with HowardSoft software).
3. Only original printed output is accepted, except for overlays, which must be copied with a high-quality output.
4. Forms must be printed on one side of paper only.

5. Overlays or preprinted pin-fed forms must be approved for the software being used. (HowardSoft has received FTB approval for its Laser-graphic or Windows-graphic printouts.)

If you cannot meet these requirements plus the additional requirements detailed later under "Printouts for the FTB," you must file a manually prepared official Form 540 instead. To aid you in this effort, the software provides non-fileable paper copies in the format of the non-computer official Form 540 when you choose to print a facsimile Form 540, or when your program settings show "No" for "Bypass alignment dots." (Alignment dots are not allowed on the scannable Form 540 because they could interfere with the special scan patch.)

Assembling the return. The FTB-preferred order for assembling the forms is:

1. Form 540,
2. Schedule W with copies of required withholding forms attached, including Forms W-2 and W-2G,
3. Schedule CA and all remaining California schedules in alphabetical order,
4. all California forms in numerical order, excluding Form 5805 and Form 5805-F
5. if required, a complete copy of the federal (Form 1040) return filed with the IRS (and, if the filing status is different on the California return, a Form 1040 recomputed using the California filing status).
6. Form 5805 and Form 5805-F.

Note that you do not have to send a copy of your federal return if you had to file only Schedules A and/or Schedule B with your federal return.

Additional rules for scannable Form 540. Because the scannable Form 540 is read by automated equipment, a number of additional rules must be followed when preparing the return for filing:

Do not use FTB address label. The software will print the taxpayer information in FTB-approved format. However, you must enter names and addresses using the same abbreviations and omission of punctuation as used on the FTB-provided address labels.

Do not make corrections on printed return. You must print the return anew if any changes are made to ensure that the computer-generated summary in the scan band is consistent with the final return.

Do not print on both sides of the paper. Only one-sided printing is allowed so that the automated equipment does not have to contend with bleed-through from the second side.

Do not include any correspondence. Even a simple transmittal letter will slow processing.

Do not file a photocopy except when using an overlay. When using an overlay, the alignment must be nearly perfect and the photocopy must be clear and dark.

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Printouts for the FTB

Do not staple payment. Contrary to former requirements to staple the payment to page 1 of Form 540, the FTB now wants you to enclose but NOT staple any payment.

Staple W-2s and 1099s, and other forms showing withholding to the NEW California Schedule W. Forms W-2 and W-2G must now be stapled to the front of the new Schedule W (California W-2 Attachment). In addition, in spite of the title for the new schedule, any other forms that show withholding, such as Forms 1099, 592-B, 593-B, and 594, must be stapled to Schedule W as well. (When you choose to print Form 540 or a complete return, the software asks if you also want Schedule W. If you answer Yes, the schedule is printed after page 2 of Form 540, as the FTB requires.)

Staple supporting forms or schedules behind Schedule W. All other attachments, including other California forms and any required federal forms, must be placed behind and stapled to Schedule W. *Be sure to place Form 5805 or 5805-F last.*

Staple Form 540 Side 2 to the entire return. You should staple ONLY side 2 of Form 540 to the rest of the return, stapling the assembly together in the upper-left corner. *Side 1 should remain loose.*

In addition, you must mail the completed return only to the special addresses shown at lines 66 and 67 of the scannable Form 540. (The address for returns with refunds, at line 66, is unique to the scannable Form 540.)

Tab adjustments are for hand-prepared Form 540 ONLY. The software is delivered with tabs for both hand-prepared and scannable Form 540 built-in. However, the tabs for the scannable Form 540 are not visible to you and are not changeable because FTB-approval of our forms depends on the built-in tabs.

| FORM 540 TABS | | |
|------------------------------|--------------------------|------|
| Enter 1=facs & FTB official: | | 1 |
| or ZERO to set tabs below: | | |
| VERTICAL- | Fiscal year to name.. | .33 |
| | Address to Your SSN... | .67 |
| in | Line 20 to line 21.... | .67 |
| inches | Ln 24 to name(pg2 top) | 1.83 |
| | Ln 71 box to SSN/PTIN. | 1.83 |
| HORIZ- | Paper edge to F/S boxes. | 1.80 |
| | ..to line 6 box..... | 7.20 |
| | ..to line 10 box..... | 6.50 |
| | ..to line 13 decimal.. | 7.80 |
| | ..to ln20 TaxTable box | 3.10 |
| | ..to ln20 FTB 3803 box | 4.70 |
| | ..to ln23 Sch. G-1 box | 2.80 |
| | ..to line 25 decimal.. | 7.80 |
| | ..to ln 28 credit name | 2.60 |
| | ..to line 28 decimal.. | 6.50 |
| | ..to ln69 FTB 5805 box | 4. |
| | ..to line 71 box..... | 7.10 |
| | ..to pd. preparer FEIN | 6.80 |

Figure CA-1. Tabs for manually-prepared form ONLY

The tab adjustments that are visible in the program settings are intended only for a hand-prepared Form 540, and not the scannable Form 540. These tab adjustments are relevant for a fill-in printout ONLY when you have set your program settings to No to "Bypass alignment dots." The tab settings as delivered (shown in Figure CA-1) provide a reasonable alignment with the official

FTB form, but alignment can never be perfect because the FTB form is *NOT* designed for computer fill-in and therefore does not follow the strict pica spacing that would make alignment good. Note that these tab adjustments affect the non-fileable facsimile printouts of Form 540. Therefore, if you change the settings for a fill-in printout, you should return them to their original settings, shown above, for an accurate facsimile printout of Form 540.

Form by Form Details

Remainder of document supplements Tax Forms Guide. Details of the tax forms are reviewed in the remainder of this document. Where details are not given here explicitly for a form or worksheet, you can refer to the main Tax Forms Guide 2005 Edition for details on the comparable federal form. Only differences from that guide are detailed here.

Control Form

Purpose. Like the federal Control Form, the state Control Form controls the automation of the software, and includes the ability to block the automatic generation of certain forms, enter prior year amounts for the penalty form, and provide custom information for the cover and billing letters. Differences between the federal and state Control Forms are largely technical, so you should refer to the separate federal Tax Forms Guide for most entries.

AUTOMATION CONTROL. This section is completely analogous to the federal Control Form, and all entries are translated from that form.

Tax year (enter 2004 or later). Although you could change this entry for California tax planning, we recommend that you do not because the California return is so closely tied to the federal return of the same tax year. Instead, you should perform tax planning with the federal return, then translate that copy of the federal return to the California return and complete tax planning with the translated return.

Monetary amounts rounded to nearest \$? It is important that you NOT change the rounding rule to No for the California return if it was Yes for the federal return, because unrounded amounts are not available for translation from a federal return that was prepared with Yes for rounding.

Block auto-creation of forms. Like the Federal Edition, you can block the automatic creation of some forms for special circumstances, but we strongly recommend against it. However, if you want the FTB to figure any underpayment penalty for you and send you a bill, you can answer Yes to "Block form 5805 auto-creation?" and the penalty will not be computed by the software. Also like the Federal Edition, certain other forms are unconditionally created when they are needed to ensure a valid return, such as Schedule D, Schedule D-1, and Schedule P Part II, because they hold results from other forms that are not otherwise posted to Form 540 or Schedule CA.

FORM 5805 CONTROL. A number of exceptions exist for the penalty for underpayments of estimated tax which have no federal parallel. It is important that you complete this section if you filed a full-year return in the prior year and had a lower tax last year. Entries from last year are NOT automatic because they are not available by translation of the federal return.

Filed full-year return for PRIOR year. This entry is translated from the federal Control Form, since you probably filed a full-year California

return if you filed a federal one, and most certainly didn't file a full-year California return if you didn't file a federal one.

2003 amounts entered for Form 5805. In order to fully automate the penalty Form 5805, amounts from the 2003 California return should be entered here from the indicated lines. If you did *NOT* file a full-year return in 2003, do NOT answer Yes to the question "2003 amounts entered for 5805," because you are not eligible for the penalty exceptions that are based on the prior-year taxes paid. Moreover, you should answer Yes here only if you actually complete the remaining lines in this section, or else the software will think that you are eligible for an exception for which you are not.

2003 AGI, tax, withholding, etc. Amounts entered here are used in Form 5805 to determine eligibility for an exception based on prior-year tax.

STATE ESTIMATED TAX PAYMENTS. The four quarterly payments are translated from the federal Control Form to these lines, then posted to line 39 of Form 540. You should not have to alter these entries if you properly completed the federal Control Form. (A payment made in January 2004 for the 4th quarterly 2003 estimated tax payment is not included, but a payment made in January 2005 for the 4th quarterly 2004 estimated tax payment is.)

Remainder of form analogous to federal Control Form. The Tax Summary is based on results on Form 540, just as the federal Tax Summary is based on Form 1040. The cover and billing letter sections provide for a date, a fee, and optional text, just like the federal Control Form. Note that the tax preparation fee at the end of the Control Form relates only to the California billing letter, so you should enter an amount only if you plan to bill separately for the California return.

Form 540 / Main Form

Form 1040 is source of entries. The “translate” feature copies a number of entries from federal Form 1040 to California Form 540. Entries that come from other California forms and schedules, however, are transferred to Form 540 only after the California return is calculated.

Tax year from Control Form. (*Road Map line, supported by Control Form.*) This entry cannot be changed, but the line provides Road Map access to the Control Form, where the tax year is set.

STEP 1, NAME AND ADDRESS. Identifying information for printouts and certain calculations is supplied here. Names, social security numbers, and address are all transferred directly from the federal Form 1040, and are used in the printout of all official forms. *CAUTION: Because the FTB-supplied label cannot be used on a scannable Form 540, your entries must match the format that the FTB uses in its address label, including abbreviations and omission of punctuation. No spaces are allowed in the first name, and no titles like Mr., Dr., or Mrs.* Additional entries appear in this section in order to generate label information in the format required by the FTB:

Apt. no. (or other type below). Although this entry is translated from the federal return, *California's format is different.* California separates the descriptor from the actual number (and/or letters), so only the number should be entered here. *Descriptors like Apt., Ste., etc., must be removed.* Furthermore, this number can be no longer than 5 characters long.

Type (Apt, Ste, Sp, Rm, Fl, Bldg, or Un). The appropriate descriptor is entered here. You will not be allowed to make an entry here if there is no entry on the preceding line. If there is an entry on the preceding line but you make no entry here, the entry APT is made for you.

Private Mailbox Number (PMB). If you use a box that is *NOT* a U.S. Postal Service box, the FTB now requires you to enter the box number separately from the main address.

Above and filing status same as 2003 Form 540? If you answer Yes, a special ** code is printed above the taxpayer's last name to tell the FTB that it can use the information from last year that is already in its computer.

PBA Code (from Schedule C, copy 1). (*auto-calc line, supported by Worksheet C*) This entry is taken from your entry for the federal Principal Business Activity (PBA) Code on the *first* copy of Worksheet C, which in turn is translated from your entry for line B of the federal Schedule C, Copy 1. This line is printed along with the taxpayer name and address at the top of Form 540, and *is now mandatory.* The FTB is authorized to disclose this PBA code, along with other personal information like SSN and address, to city tax officials under specific limited circumstances. *CAUTION: If you will print using Laser-graphic or Window-graphic forms, you must make sure*

that the 6-digit code on Worksheet C, copy 1, contains no spaces so that the code is printed in the proper format for the scannable Form 540. Spaces are appropriate only for a manually completed Form 540, in which you use the FTB form with hand-print boxes.

Special handling. Additional entries not found on the federal Form 1040 are provided for further conformance with the FTB requirements for printing in the address label area of the scannable Form 540:

DISASTER LOSS? If you answer Yes, the word DISASTER appears to the right of your ZIP code in the address label area of a scannable Form 540. You must itemize here to explain your claim for special handling, providing details of the disaster.

MILITARY? If you answer Yes, the word MILITARY appears to the right of your ZIP code in the address label area to indicate special handling to the FTB. Itemize this line to explain.

If YOU deceased, date (mm-dd-yy). Although this entry is translated from the federal return (starting with release 2005.02), the formatting is somewhat different on the printouts. This entry is printed in the format "(DECD mm-dd-yy)" to the right of the taxpayer's name on a scannable Form 540. (*NOTE: If the surviving spouse is preparing the return and has not remarried during the tax year, enter "Surviving spouse" next to the signature on Form 540.*)

If SPOUSE deceased, enter date. This entry is printed in the format "(DECD mm-dd-yy)" to the right of the spouse's name on a scannable Form 540.

Executor, Guardian, etc. If the taxpayer is deceased or not capable of preparing the return, enter the name of the responsible person here. This name is printed to the right of your entry for "Additional address information" on the scannable Form 540.

Representative type (1=Administrator, 2=Beneficiary, 3=Executor, 4=Spouse, 5=Trustee). If the taxpayer is deceased and you are signing the return, identify here the type of representative you are. Otherwise, leave the entry at zero. (*This entry is used only on e-filed returns.*)

STEP 2, FILING STATUS. Type 1=Single, 2=Married Filing Jointly, 3=Married Filing Separate, 4=Head of Household, 5=Qualifying Widow(er). This entry is transferred from the federal return and should NOT normally be changed. By California law, your filing status on Form 540 MUST be the same as your filing status on Form 1040 with only two exceptions:

A if federal filing status is Married Filing Jointly and either spouse was an active member of U. S. armed forces (or an auxiliary), for California returns you may file either jointly or separately, and

B if federal filing status is Married Filing Jointly and either spouse was a non-resident and had no California income for the entire 2004 tax year, you may file separately on Form 540 (but if you file jointly you must use Form 540NR, a form designed for non-residents which is not built into our software).

If the filing status on the California return is different from that on the federal return, you will have to recompute the federal AGI based on the California filing status and data. You must submit BOTH the official Form 1040 and the recomputed Form 1040 with your Form 540 return.

STEP 3, EXEMPTIONS. The qualifications are the same as those for the federal return, and are therefore transferred here automatically from line 6 of Form 1040 during the translation of the federal return.

YOU dependent on another's return? Translated from your answer to the same question on the federal Control Form.

SPOUSE dependent on another's return? Translated from your answer to the same question on the federal Control Form.

6 Dependent on another's return? *(auto-calc)* Automatically Yes if either of the above two answers is Yes. Like the federal return, a Yes answer affects the standard deduction for low-income taxpayers and results in no personal exemption for the taxpayer.

7 Personal. *(auto-calc)* Normally one if single, married filing separately, or head of household, and two otherwise; but one less than these counts for each person who is claimed as a dependent on another person's return.

\$ amount of credit for line 7. *(auto-calc)* Computed as \$85 times the preceding number, this amount may be reduced at line 21 for high-income taxpayers.

YOU blind at year-end? Translated from your answer to the same question on the federal Control Form.

SPOUSE blind at year-end? Translated from your answer to the same question on the federal Control Form.

8 Blind. *(auto-calc)* Computed as the number of Yes answers on the preceding two lines. *You must attach a doctor's statement the first year a blind claim is made.*

\$ amount of credit for line 8. *(auto-calc)* Computed as \$85 times the preceding number, this amount may be reduced at line 21 for high-income taxpayers.

Ages at year-end. The age entries are used to determine eligibility for the senior exemption at line 9 of Form 540, eligibility for senior head of household credit in Part III of Schedule P, and various special calculations for children under 14. (The ages are translated from your age entries on the federal Control Form.)

YOU are 65 or more at year-end. *(auto-calc)* Answered based on the preceding age entry.

SPOUSE is 65 or more at year-end. *(auto-calc)* Answered based on the preceding age entry.

9 Senior. *(auto-calc)* Computed as the number of Yes answers on the preceding two lines.

\$ amount of credit for line 9. *(auto-calc)* Computed as \$85 times the preceding number, this amount may be reduced at line 21 for high-income taxpayers.

10 Total number of dependents. *(Supported by the Dependents Worksheet.)* The names and relationships on the translated worksheets are taken directly from the corresponding worksheets for federal return. However, due to the different design for the federal Form 1040 compared with the California Form 540, the federal worksheets have separate 10-character entries for first and last name, whereas the California worksheets have a single 15-character entry. As a result, the last name may be truncated during the translation, so you may prefer to reenter the name with a different abbreviation.

Total dependent exemption credit. *(auto-calc)* Computed as \$265 times the preceding number, this amount may be reduced at line 21 for high-income taxpayers.

11 Add line 7 through line 10. *(auto-calc)* Computed as the sum of monetary amounts on lines 7, 8, 9, and 10.

The result on line 11 is used in computing the exemption credits at line 21 of Form 540.

STEP 4, TAXABLE INCOME. Taxable income is computed from the federal AGI and deductions with certain adjustments from Schedule CA taken into account.

YOUR and SPOUSE state wages (W-2). *(Supported by W-2 Worksheets.)* A separate set of worksheets is provided for each spouse. They are translated from the federal W-2 worksheets that support lines 7a and 7b of Form 1040. W-2 wages reported on the federal W-2 Worksheets are posted to both the federal and State lines of the State W-2 Worksheets. CAUTION: If the State wages in box 16 of your W-2 differs from the federal wages in box 1, you MUST reenter the State amount on line 16 of the State W-2 Worksheets. (Wages earned in ALL states combined must be entered, not just those earned in California. Double-taxed income is adjusted on Schedule S.)

YOUR and SPOUSE federal wages. *(auto-calc lines)* Taken from box 1 of all W-2 worksheets, separately for you and spouse.

YOUR and SPOUSE California tax withheld. *(auto-calc lines)* The amount from box 17 of the federal W-2 Worksheet is translated to the line "California tax withheld," and the totals are carried to Form 540 for use in computing line 38. If the translated amount includes payments to other states, you must remove the withholding for other states from the California W-2 worksheets.

YOUR and SPOUSE California SDI wages. *(auto-calc lines)* Taken from box 16 of the W-2 Worksheet but limited to no more than \$68,829 for each worksheet, this is the amount legally deducted by all employers combined. If this amount exceeds \$68,829, you may have a deduction at line 41 for excess SDI.

YOUR and SPOUSE California SDI withheld. *(auto-calc lines)* The amount on the federal W-2 Worksheet line labeled "Other non-fed tax (boxes 14 & 21)" is translated to the SDI line on the California

W-2 Worksheet. *CAUTION: If the translated amount includes payments to other states or localities, you must remove those amounts from the California W-2 worksheets.* The maximum for which you are liable is 1.18%% of all state wages combined up to a maximum of \$68,829 for wages paid in 2004. Any excess is automatically claimed at line 41 of Form 540. (Note that any one employer who deducts more than the prescribed percentages or applies the percentages to more than \$68,829 of your wages from that employer must reimburse you for any excess. You cannot claim an excess from any one employer on line 41. The software ensures that over-withholding by any one employer is not included in line 41 *as long as you view each and every W-2 worksheet before completing the return.*)

12 State wages from Form W-2. (*auto-calc*) Computed as the sum of state wages above for you and spouse.

Other earned income in Schedule CA, line 7. (*Road Map line, supported by Schedule CA.*) Other earned income that is included in line 7 of Form 1040, but not on W-2 Worksheets, appears here, as adjusted on Schedule CA.

Earned income on worksheet C. (*Road Map line, supported by Worksheet C.*) Originally taken from federal Form 1040 line 12, adjustments on California Worksheet C may change this entry.

Earned income on worksheet E. (*Road Map line, supported by Worksheet E.*) Originally taken from the Partnership/S-corp Worksheets on Schedule E, adjustments on California Worksheet E may change this entry.

Earned income on worksheet F. (*Road Map line, supported by Worksheet F.*) Originally taken from federal Form 1040 line 18, adjustments on California Worksheet F may change this entry.

Other earned income in Schedule CA, line 21. Translated from federal Form 1040, you may need to change the translated amount if you made any adjustments in line 21 of Schedule CA that affect California earned income. (This amount is *NOT* automatically taken from Schedule CA because the earned income part of adjustments on line 21 of Schedule CA is *NOT* separately identified.)

Total California earned income. (*auto-calc*) Sum of the above six lines (the state wages from Form W-2 plus the other five lines of earned income). This total is used in special calculations on Schedule P.

Total federal earned income. This amount is translated from the earned income totals that appear below line 22 of the federal Form 1040. It will often differ from the state amount when you have self-employment income because half the federal self-employment tax is used to reduce earned income for federal purposes, but there is no similar deduction for the state. Earned income is used in determining the proper standard deduction for dependent filers at line 18. The earned income from Worksheets C, E, and F are used in Schedule P

as well, to determine whether you are excepted from the minimum tax because your business income is less than \$1 million.

13 Federal AGI on Form 1040, line 36. Automatically taken from Form 1040 as indicated. *CAUTION: If the filing status on the California return is different from that on the federal return, you will have to recompute the federal AGI based on the California filing status, and enter the revised amount here.* The only legitimate cases for a difference in filing status is married filing jointly vs. married filing separately, and vice versa, in order to minimize the tax on both returns, and only if either spouse was an active member of the U.S. armed forces (or auxiliary) or was non-resident and had no California income for the entire 2004.

14 California adjustments -- subtractions. *(Road Map line, supported by Schedule CA.)* Schedule CA is the collection point for adjustments for all investments, businesses, and itemized deductions. The total *subtractions* from AGI due to differences between federal and state law are posted here from Schedule CA based on the results in columns B and C of line 36 of Schedule CA.

15 Subtract line 14 from line 13. *(auto-calc)* Computed as indicated, allowing both negative and positive results.

16 California adjustments -- additions. *(Road Map line, supported by Schedule CA.)* The total *additions* to AGI due to differences between federal and state law are posted here from Schedule CA based on the results in columns B and C of line 36 of Schedule CA.

17 California adjusted gross income. *(auto-calc)* Computed as line 15 plus line 16.

If Married Filing Separately, does spouse itemize? Taken from line 35b of Form 1040, a Yes answer will cause itemized deductions to be used whether or not the standard deduction is more, because both you and spouse must make the same election -- that is, both must use itemized deductions or both must use the standard deduction.

Itemized deductions on Schedule CA. *(Road Map line, supported by Schedule CA.)* The amount of federal itemized deductions modified by California adjustments is posted here from line 42 of Schedule CA.

Standard deduction. *(auto-calc)* The standard deduction for 2004 is \$3,165 for taxpayers filing single or married filing separately, and \$6,330 for all others, but special limitations apply for dependent filers (which are automatically applied by the software).

Itemized deductions used. *(auto-calc)* This entry is automatically Yes when itemized deductions exceed the standard deduction as long as you answered No to the question below line 17, "If MFS, spouse itemizes?"

18 California standard or California itemized deduction. *(auto-calc)* When the preceding answer is Yes, the itemized deductions from

Schedule CA are used here. Otherwise the standard deduction is used.

Taxable income to Schedule P. (*auto-calc*) Computed as line 17 less line 18, allowing a negative result when line 18 exceeds line 17 as required for calculations on Schedule P.

19 Taxable income. (*auto-calc*) Computed as line 17 less line 18, but no less than zero.

The tax is computed on the basis of this adjusted taxable income.

STEP 5, TAX. Tax computations are figured separately from the federal tax, but the method is similar.

from Tax Table. (*auto-calc*) Normally computed from the FTB instructions for Tax Table in the Form 540 instructions, but zero if an amount from Form 3800 appears below.

Tax rate schedule choice gone. The label for the preceding line is somewhat misleading because it is *really* based on *either* the tax table or the tax rate schedule. However, the FTB has cleverly eliminated the need for the tax rate schedules by revising the instructions so that a simple modification of the top table amount (the tax on \$81,750 of income) is used. See page 18 of the FTB Form 540 Instructions for details. (Formerly, you had to compute tax based on the tax rate schedules shown in Table CA-2, page CA-4, when taxable income exceeded \$100,000. Now you are instructed to follow a simpler procedure that produces the same result rounded to the nearest dollar.)

from FTB Form 3800. (*Road Map line, supported by Form 3800.*) If a Form 8615 existed on the federal return, Form 3800 will exist on the California return automatically. The result, however, is assured of full validity only upon the final recalculation of the return. Any result that appears here is used in line 20 in place of any other tax results.

from FTB Form 3803. (*Road Map line, supported by Form 3803.*) If you chose to include a child's interest and dividend income in your own income rather than filing a return for the child, you must use Form 3803 to determine the amount of additional tax you owe. It is fully analogous to federal Form 8814, and produces an additional tax for most parents. (Some taxpayers choose to file a return for the child, even though it involves additional work, because it generally results in a slightly lower combined tax for the child and parent.)

20 Tax. (*auto-calc*) Computed as either the tax table or Form 3800 amount, whichever applies, plus the add-on tax from Form 3803. An X will appear in the box on the printed Form 540 for the tax method(s) used.

21 Exemption credits. (*auto-calc lines*) Exemption credits are determined automatically based on the number of exemptions appearing on lines 7, 8, 9, and 10. In the simplest case, the credit is just the amount on line 11. When this simple case applies, a Yes appears beside the line labeled "Exemptions from: Line 11." But for those with higher incomes, special limitations apply. When the high in-

come limitation applies, a Yes appears beside the line labeled "AGI Limit worksheet" and the credit is computed based on a scheduled phaseout of credits for high federal AGI. (The phaseout starts at a federal AGI of \$139,921 for single and married filing separately, \$209,885 for head of household, and \$279,846 for married filing jointly or qualifying widow(er). The former alternative minimum tax limitation no longer applies.)

22 Subtract line 21 from line 20. *(auto-calc)* As indicated, but no less than zero.

23 Tax from Schedule G-1 and Form 5870A. Line 23 is comprised of two entry lines for additional special taxes from forms not built into the software. Tax from Schedule G-1, line 30, is the FTB equivalent of federal Form 4972 for taxing lump sum distributions from qualifying retirement plans. Tax from Form FTB 5870A is the additional tax on accumulation distribution of trusts from Form 5870A. *(Both forms are built into the software for the Premium Level.)*

24 Add line 22 and line 23. *(auto-calc)* As indicated.

The result on line 24 is automatically carried to line 25 in the next step.

STEP 6, CREDITS. Numerous credits are available by California tax laws that have no parallel by federal tax law.

25 Amount from Side 1, line 24. *(auto-calc)* As indicated.

Itemize here for Schedule P, Page 2. *(Road Map line, supported by Schedule P Page 2.)* Schedule P, page 2 is used to consolidate credits from numerous sources. The credit names and amounts are automatically posted to lines 28 and 29 for the first two credits claimed. The total of all other credits is posted to line 30, and the FTB must see Schedule P for details.

Itemize here for Form 3540. *(Road Map line, supported by Form 3540.)*

Form 3540 is an additional form for consolidating credit carryovers. If no Schedule P exists for the return, any credit carryovers entered on Form 3540 are posted here in the same way as described for Schedule P, above. However, if more than two credits are claimed, you *MUST* use Schedule P, so the software will automatically generate Schedule P in this case, based on the entries on Form 3540.

28 through 30, Credit names, codes, and amounts. *(Auto-calc lines, supported by Schedule P Page 2 and Form 3540.)* Credit names and amounts are posted here from Form 3540 or Schedule P Page 2 as described above.

Number qualified for renter's credit. The FTB provides a full page of instruction to help you determine if you are qualified in their 2004 Personal Income Tax Booklet (listed in their Table of Contents under the heading *Nonrefundable Renter's Credit Qualification Record*). Qualifications include being a resident of California for the entire 2004 tax year and paying rent for at least half the year on your principal residence in California. Qualifications based on income and filing status are enforced at the next line.

Tentative renter's credit. *(auto-calc)* The nominal credit is \$60 times the preceding number. However, the credit is disallowed if California AGI on line 17 is more than \$29,955 if single or married filing separately (\$59,910 for all other filing statuses). *HINT: If married filing separately and both spouses lived in the same rental property and qualified for the credit, one spouse may claim the entire \$120 (with the other spouse claiming none) rather than both claiming \$60.*

31 Nonrefundable renter's credit. *(auto-calc)* For most taxpayers this line will be the same as the preceding line. However, the credit may be limited by tentative minimum tax on Schedule P. Therefore, if a Schedule P exists for the return, the limited amount is taken from column (b) of line 16 of Schedule P, page 2.

33 Total credits. Add lines 28 through 31. *(auto-calc)* As indicated.

IRC Section 453 or 453A interest. If you owe interest on deferred tax from installment obligations, enter the amount of additional tax here. The special rules that impose this interest apply to nondealer sales exceeding \$150,000. An entry here will cause the phrase "IRC Sec 453A int." to be printed beside line 34 with the amount.

34 Subtract line 33 from line 25. *(auto-calc)* Computed as indicated, plus the above special tax, but no less than zero.

STEP 7, OTHER TAXES. Two additional taxes are reported here:

35 Alternative minimum tax (Schedule P). *(Road Map line, supported by Schedule P, Page 1.)* Although Schedule P is automatically created and completed upon final recalculation of the return when needed, you will generally have to access the schedule yourself if you have any tax preferences other than the ones on Schedules A and D, such as accelerated depreciation or depletion.

Tax on IRAs and other qualified retirement plans: Form 3805P. *(Road Map line, supported by Form 3805P.)* California law conforms to federal law for the tax on early distributions, but the penalty percentage is different and other differences apply. You must complete Form 3805P, Part I, which is the FTB equivalent of federal Form 5329, Part I, to determine the proper entry for this line. If an entry appears on this line, and none appears on the next line, the code "3805P" is printed on the Official Form 540 to the left of line 36 to indicate to the FTB that the total for line 36 is a tax from this form. (If there is an entry on the next line as well, this code will appear in a supporting statement for line 36.)

Additional taxes from OTHER. This line is provided for other taxes, including the recapture of various credits from the following FTB forms (not built into the software):

Forms 3501, Employer Child Care Program/Contribution Credit *(built into the software for the Premium Level),*

Forms 3535, Manufacturers' Investment Credit,

Form 3805Z, Enterprise Zone/Program Area Deduction and Credit Summary (*built into the software for the Premium Level*),

Form 3806, Los Angeles Revitalization Zone Deduction and Credit Summary (*built into the software for the Premium Level*),

Form 3807, Local Agency Military Base Recovery Area Deduction and Credit Summary,.

Form 3808, Manufacturing Enhancement Area Credit Summary, and

Form 3809, Targeted Tax Area Deduction and Credit Summary.

You must identify the source of the tax in a supporting statement for this line showing the appropriate code (such as 3501, 3535, etc.) in the description column and the dollar amount in the amount column, so that the sources will be identified to the left of line 36 on the Official Form 540, as required by the FTB.

36 Other taxes. (*auto-calc*) Computed as the sum of the preceding two entries.

37 Total tax. Add lines 34 through 36. (*auto-calc*) Computed as the sum of lines 34 through 36.

STEP 8, PAYMENTS. Withholding and other tax payments already made are reported here.

California income tax withheld on Form W-2. (*auto-calc*) Computed as the sum of California income tax withheld for you and spouse, as reported on W-2 worksheets attached to the lines above line 12.

California income tax withheld on Form W-2G. If there was any California state income tax withheld on any Forms W-2G (Gambling Winnings) received for 2004, you must enter that amount here (as shown in box 10 of Form W-2G).

California income tax withheld on Form 1099-R. If there was any California state income tax withheld on any Forms 1099-R (Distributions from Pensions, Profit-Sharing Plans, IRAs, etc.) received for 2004, you must enter that amount here (as shown in box 10 of Form 1099-R). (*This amount is translated from the federal return based on your entries on 1099-R worksheets for federal Form 1040 lines 15 and 16.*)

California income tax withheld elsewhere (itemize). If any other California income tax was withheld for 2004 and not included in the preceding three lines, such as "backup withholding", enter that amount in a supporting statement for this line, identifying the form on which it was reported to you (e.g., Form 1099-MISC, Form 1099-INT, Form 1099-DIV, etc.)

38 California income tax withheld. (*auto-calc*) Computed as the sum of the above three lines.

Tax applied from 2003. Enter the amount identified on the prior-year California return as the part of any refund to apply to 2004 estimated tax payments.

Quarterly estimated tax payments. (*Road Map lines, supported by Control Form.*) The four quarterly payments for California estimated

tax for 2004 are taken from the corresponding lines on the Control Form.

Tax paid with Form FTB 3519. (*Road Map line, supported by Form 3519.*) Although you no longer have to formally apply for a filing extension, you must remit any tax due by the regular April 15 filing deadline with a payment voucher, FTB 3519. (*HINT: If you have payments other than those from FTB 3519 to report here, such as California estimated tax payments made on your behalf by an estate or trust, you must NOT create a Form 3519 for this return because the result from Form 3519 would overwrite any entry you make here.*)

39 2004 estimated tax payments and amount applied from 2003 return. (*auto-calc*) Computed as the sum of the above six tax payment entries. The separate amounts are also used in the automation of Form 5805, excluding the payments with the filing extension.

40 Real estate withholding. The withholding for this line should appear on a Form 597, 592-B, or 594 you receive when you sell real estate in California. Enter the California withholding here, and attach a copy of the referenced form(s) to the new Schedule W that automatically prints with Form 540 (unless you request otherwise when you choose to print).

41 Excess California SDI withheld. (*auto-calc*) Computed as the excess withheld because of withholding from more than one employer based on the the FTB's Excess SDI (or VDPI) Worksheet, using amounts entered on our W-2 Worksheets.

Child and Dependent Care Expenses Credit. This credit is similar to the federal credit on Form 2441, but the percentages are different and some of the rules are different. The credit is claimed on Form 3506, which is translated from federal Form 2441 and accessible by itemizing line 44 or line 45.

42 SSN of 1st qualifying child. (*auto-calc, supported by Form 3506*) The SSN of the first child you identified on Form 3506 appears here after you view the worksheets for Form 3506.

43 SSN of 2nd qualifying child. (*auto-calc, supported by Form 3506*) The SSN of the second child you identified on Form 3506 appears here after you view the worksheets for Form 3506.

44 Federal child care credit. (*Road Map line, supported by Form 3506.*) Form 3506 is translated from the federal Form 2441, and the California form deviates little from the intent of the federal form. As a result, the credit is nearly automatic for most taxpayers. However, there are additional questions you must answer on Form 3506, including California residency questions, and you MUST view the translated worksheets at line 2 of Form 3506 so that the children's SSNs will appear on lines 42 and 43, above. The amount that appears on this line is generally the same as the credit on federal Form 2441. However, no limitation to federal tax is applied for the purposes of this form.

45 California child care credit. (*Road Map line, supported by Form 3506.*) Taken from Form 3506, this credit is generally 50% of the federal credit for California AGI up to \$40,000, 43% from \$40,000.01 to \$70,000, 34% from \$70,000.01 to \$100,000, and zero above \$100,000.

46 Total payments. Add lines 38, 39, 40, 41, and 45. (*auto-calc*) Computed as indicated.

STEP 9, OVERPAID TAX OR TAX DUE. Preliminary results are summarized here.

47 Overpaid tax. (*auto-calc*) Computed as line 46 less line 37, but no less than zero.

2005 estimated tax from Form 540-ES. (*Road Map line, supported by Form 540-ES.*) This line is not a part of the Official Form 540, but is provided to access Form 540-ES for determining the estimated tax payments required for the next tax year. The amount shown here is the total estimated tax due. If you plan to apply any or part of the excess payment on line 47 to estimated tax payments for 2005, the percentage you enter below will control the maximum amount to be applied. If you complete no Form 540-ES but you want to apply some of the refund to next year's estimated tax, enter 100% below and the dollar amount to apply here. HINT: If you know beforehand that you will want to apply the *entire* refund, you can enter any unreasonably large amount here to force the application, since this line is not printed on the Form 540 that is filed with the FTB.

Percent of above estimated tax to prepay. This entry controls the amount of any overpayment appearing on line 47 that will be applied to 2005 estimated taxes via line 48, below. If you complete a Form 540-ES, you will typically enter 25% here so that the first quarter's estimated tax payment is automatically made. Or, if you prefer, you could pay up to the amount of estimated taxes for the entire year by entering 100% here.

48 Amount of line 47 to apply to your 2005 estimated tax. (*auto-calc*) Computed as the lesser of the above percentage of the 540-ES estimate and the amount on line 47, but zero if the result is less than \$5.

49 Amount of overpaid tax available this year. (*auto-calc*) Computed as line 47 less line 48.

50 Tax due. (*auto-calc*) Computed as line 37 less line 46, but no less than zero.

51 Use Tax. For out-of-state purchases only, enter the sales tax that would have applied if you had bought the item in California, but reduced by any sales tax you paid to the other state for the item.

STEP 10, CONTRIBUTIONS. California provides for a means for you to contribute directly to certain special state funds. Contributions to the first fund are limited to the amount of senior exemption claimed on line 9.

You and/or spouse elects to contribute to Seniors Special Fund? Anyone who claims the seniors' exemption credit on line 9 can contribute any even dollar amount up to a maximum of his or her exemption to this special fund, which provides services and advocacy for seniors. Your entries are therefore rounded to even dollar amounts and limited to no more than \$85 for each spouse, and your entry is zeroed for any spouse who does not claim a senior exemption on line 9.

52 California Seniors Special Fund. *(auto-calc)* Computed as the sum of the above two entries for you and spouse.

Contributions to the remaining funds can be made in any *whole dollar* amounts. Your contributions will increase the tax you owe (or decrease your refund) by the amount of the contribution.

53 Alzheimer's Disease Fund. For researching the cause, cure, and treatment of Alzheimer's disease and related disorders.

54 California Fund for Senior Citizens. For direct services to senior citizens and to support the California Senior Legislature.

55 Rare and Endangered Species Program. For the conservation of endangered and rare fish, wildlife, and plants.

56 State Children's Trust Fund for Prevention of Child Abuse. To fund programs for the prevention of child abuse and neglect.

57 California Breast Cancer Research Fund. To fund programs for the cure, screening, and treatment of breast cancer.

58 California Firefighters' Memorial Fund. For the construction of a memorial to California firefighters at the state capitol.

59 Emergency Food Assistance Program Fund. To help local food banks feed hungry people in California.

60 California Peace Officer Memorial Foundation Fund. To maintain and annually update a memorial on State Capitol grounds.

61 Asthma and Lung Disease Research Fund. To provide grants for research on the causes of lung disease.

62 California Missions Foundation Fund. To restore and repair the Spanish colonial and mission era missions in California and preserve their artworks and artifacts.

63 California Military Family Relief Fund. To aid members of the California National Guard who are called to active duty.

64 California Prostrate Cancer Research Fund. To fund research for prostrate cancer.

65 Total contributions. *(auto-calc)* Computed as the sum of lines 52 through 64.

Note that these contributions are not deductible on the return, but are merely a direct means of contributing to the funds.

STEP 11, REFUND OR AMOUNT YOU OWE. The Voluntary Contributions are reflected in the final amounts below.

66 REFUND or NO AMOUNT DUE. *(auto-calc)* Computed as line 49 less line 51 and less line 65, but no less than zero.

67 AMOUNT YOU OWE. (*auto-calc*) Computed as line 50 plus line 51 plus line 65 less line 49, but no less than zero.

Note that the penalties in Step 12 are not reflected in these amounts, so the actual amount to be paid to the FTB may be more.

STEP 12, INTEREST AND PENALTIES. The FTB will generally compute penalties for you and bill you, but you can get a complete picture of the tax bite by reflecting them here yourself.

68 Interest, late return penalties, and late payment penalties. Enter here only the amount included in the payment enclosed with the return that is to be applied to any late penalties and interest. This is *NOT* the penalty for underwithholding or underpayment of estimated tax, but the penalties and interest for not filing or paying on time. Interest is charged for taxes not paid by April 15th and an additional penalty is charged for not filing by October 17th (the extension filing date). The interest is typically 5% of the tax not paid plus ½% per month or part thereof that the return is late. The late filing penalty is generally 25% of the tax not paid. In addition, interest is charged on the penalties until they are paid at rates that are adjusted twice a year by the FTB.

Is Form 5805 attached? (*auto-calc, supported by Form 5805/5805-F.*) Automatically Yes if a Form 5805/5805-F exists for the return and you do *NOT* qualify for 5805-F.

Is Form 5805-F attached? (*auto-calc, supported by Form 5805/5805-F.*) Automatically Yes if a Form 5805/5805-F exists for the return and you qualify for 5805-F because of your farm income.

69 Underpayment of estimated tax (Form 5805). (*Road Map line, supported by Form 5805.*) Form 5805 is automatically generated when a penalty may exist, unless you answered No to the auto-create question in the first section of Form 540. However, if you are a farmer or fisherman, you should supply additional information on Form 5805 so that the software can determine whether you qualify for the more liberal Form 5805-F. (You need not complete Form 5805 or 5805-F if you want the FTB to figure the penalty for you and send you a bill.)

70 Total amount due. (*auto-calc*) Computed as line 50 plus lines 65, 68, and 69 less line 49, but no less than zero, this is the total check that must be written to the Franchise Tax Board, not just the amount on line 67.

71 Forms NOT needed next year? (*Relevant for manually-prepared Form 540 only.*) Answer Yes if you do NOT need the FTB to send you income tax forms next. If you answer Yes you will receive only a mailing label for your use when mailing next year's return, and no forms nor FTB instructions. *Note that this question and its answer does not appear on the scannable Form 540 that is printed by the software. The FTB automatically assumes that those who use computer-generated forms will not need forms from the FTB next year.*

Are you paying the full amount due? You may choose to pay less than the full amount due, and penalties will apply only to the balance not paid. If you will be paying the full amount shown on the preceding line, answer Yes here.

Amount to be paid. If you answered Yes above, the total due appears here. But if you answered No, you must enter the amount you will pay. If you choose a direct debit from your account, below, this is the amount by which your account will be debited.

STEP 13, DIRECT DEPOSIT INFORMATION. Complete the following lines to direct the FTB to deposit any refund directly in your account.

Routing number. This number tells where to send a wire transfer of funds. If a checking account, the number is the first set of computer numbers printed at the bottom of your checks, and should be 9 digits long. Otherwise you must get the number from your bank.

Account Type: Checking? You must identify whether the account to which you want the refund deposited is a checking account or a savings account. However, if you do not supply a routing number, above, of at least 9 characters length, a Yes answer will not be allowed here and both this and the next entry will be No. *(For e-file, if you chose a RAL or QIK funds on Form 8453, the routing number for the bank that processes the RAL or QIK appears above and a Yes answer appears here.)*

Account Type: Savings? *(auto-calc)* Automatically the opposite of the preceding answer if you entered a routing number of at least 9 characters, and No otherwise.

Account number. Enter full account number, including the bank's branch number. If a checking account, the number is the second set of numbers printed at the bottom of your checks. (Be sure not to include the last set of numbers, which is your check number.)

Above account information accepted. *(auto-calc)* Incomplete information will not be accepted by the FTB. This answer therefore highlights to you whether anything is missing in your entries. For example, the routing number must be 9 digits starting with 01 through 12 or 21 through 32, you must identify the type of account by a Yes for either checking or savings, and you must enter an account number. Otherwise a No will appear here and your claim for direct deposit will be rejected.

FEDERAL RETURN REQUIREMENT. This section warns you of the need to send a copy of your federal return with the California return.

Fed return attachment required. *(auto-calc)* Automatically Yes if the return contains a California Worksheet C, E, or F, a California Schedule D, D-1, or P, or a California Form 3800, 3801, 3805E, 3805P, or 3885A. You MUST send a copy of the federal return when you file the California return if this answer is Yes.

Print above answer on Form 540? Answer Yes if you want the above answer printed in the boxes provided for it near the top of a scan-

nable Form 540. The option not to print the answer is provided because the completion of the boxes is optional, according to the FTB. If you have followed the Road Map in completing the return, itemizing to supporting forms as needed, your return is complete by the time you reach this point. A final recalculation (which is automatic) may be required, however, before the results on the screen reflect the final return.

Schedule CA / California Adjustments

Collection point for all adjustments to federal AGI. This schedule consolidates the differences between federal and California amounts for most federal forms and schedules. The line numbers follow those for federal Form 1040. Results from all investment and business activities flow through this form, including all adjustments to the amounts on federal Schedules A, B, C, D, E, and F, and Forms 2106, 2119, 3903, 4562, 4684, 4797, 4835, 6252, 8582, and 8829. Other income and deductions treated differently by California are also reported here.

PART I, INCOME ADJUSTMENT SCHEDULE. The first part collects all differences that affect California AGI. Each line contains three parts: column A for amounts on federal Form 1040, column B for amounts to be subtracted from A for California returns, and column C for amounts to be added to A for California returns.

Section A -- Income. The first section corresponds to the income section of Form 1040.

Federal W-2 wages in Form 1040, line 7. (Auto-calc line, supported by Form 540.) The sum of federal wages for you and spouse, taken from the W-2 Worksheets that support line 12 of Form 540, is posted here.

California adjustment to federal wages. This entry should be zero for most taxpayers. There are only a few special items that justify an entry here, as detailed in the FTB instructions for line 7 of Schedule CA. CAUTION: This was an auto-calc line in releases prior to 2005.02b, computed as the difference between the State W-2 wages shown on line 12 of Form 540 and federal W-2 wages above, but this was inappropriate. In California, ALL wages are taxable, including those earned in other states. (The potential for double taxation is then handled through California's Schedule S in which you are given credit for taxes paid to other states.)

Other income in Form 1040, line 7. The next few lines are translated from the special extra lines that contribute to the line 7 total in our Form 1040. They are amounts that are treated like wages by the IRS but are *NOT* reported to you on a W-2 form, such as certain taxable scholarships and excess reimbursements from employers for employee expenses, child care, and moving expenses.

Federal other income in line 7. (auto-calc) This is the sum of the above other income not reported on W-2 forms.

California adjustments to other income. This adjustment line is provided to reflect differences between federal and California law for active-duty military pay, ride-sharing benefits, sick pay received under the Federal Insurance Contributions and Railroad Unemployment Insurance Acts, income exempted by U.S. treaties, and federal source income under IRC Section 911. Note that California allows a subtraction from income for graduate-level education expenses paid

by employers if that income was taxable on the federal return. (A positive entry on the adjustment line is used in column C as an addition, and a negative entry is used in column B as a subtraction.)

- 7 Wages, salaries, tips, etc.** (Auto-calc lines, supported by Form 540.) The first part of this line is the amount for column A, computed as the "W-2 wages in Form 1040, line 7" plus the "Other income in Form 1040, line 7," this amount appears in column A of Schedule CA, and represents the amount actually reported on the federal form. The remaining two parts are computed from the California W-2 wages ("Federal W-2 wages in 1040 line 7" plus "California adjustment to federal wages") plus the "California adjustment to other income." A negative adjustment appears in column B and a positive adjustment appears in column C.
- 8 Taxable income and tax-exempt interest.** (Road Map lines, supported by Worksheet B.) These lines reflect interest taxed on the federal return but not the California return, such as excluded U.S. savings bonds and treasury bills, and interest taxed on the California return but not the federal return, such as state and municipal bonds for areas outside of California, as identified on the 1099-INT Worksheets for the federal Schedule B.
- 9 Dividend income.** (Road Map lines, supported by Worksheet B.) These lines reflect dividends taxed differently on the federal return than the California return, as identified in Worksheet B.
- 10 State tax refund.** Column A is translated from Form 1040, line 10, and is the state income tax refund or tax rebate you received in the tax year and included as income on the federal return. The amount is automatically posted to column B because a state refund is not income on a California return (because the corresponding overpayment was not deductible on the California return).
- 11 Alimony received.** Column A is translated from Form 1040, line 11. You must enter an amount in column C if a nonresident alien and received any alimony not reported on federal Form 1040, line 11.
- 12 Business income or (loss).** (Road Map lines, supported by Worksheet C.) The total on federal Form 1040, line 12, is translated to column A, and adjustments resulting from Worksheet C, which relates to federal Schedule C, are posted to columns B and C.
- 13 Capital gain or (loss).** (Road Map lines, supported by Schedule D.) The total on federal Form 1040, line 13, is translated to column A, and adjustments resulting from Schedule D are posted to columns B and C.
- 14 Other gains or (losses).** (Road Map lines, supported by Schedule D-1.) The total on federal Form 1040, line 14, is translated to column A, and adjustments resulting from Schedule D-1 are posted to columns B and C.
- 15a and 15b, IRA distribution and Taxable amount.** Because California law differed from federal law before 1987 on the amount of IRA

contributions that could be deducted, the amount that is taxed when you receive benefits can often be less on a California return. You would therefore generally have a subtraction for column B. The gross distribution and the taxable amount for column A are translated from the federal Form 1040, lines 15a and 15b, but you must make any required adjustments to the taxable amount in columns B and C. See FTB Pub. 1005 for details.

16a and 16b, Pensions & annuities and Taxable amount. Even though California uses similar methods for computing the taxable amount, differences exist depending on when contributions were made to the pensions and annuities. The gross distribution and taxable amount for column A are translated from federal Form 1040, lines 16a and 16b, but you must make any required adjustments to the taxable amount in columns B and C. See FTB Pub. 1005 for details.

17 Rentals, royalties, partnerships, estates, trusts, etc. (*Road Map lines, supported by Worksheet E.*) The total on federal Form 1040, line 17, is translated to column A, and adjustments resulting from Worksheet E, which relates to federal Schedule E, are posted to columns B and C.

18 Farm income or (loss). (*Road Map lines, supported by Worksheet F.*) The total on federal Form 1040, line 18, is translated to column A, and adjustments resulting from Worksheet F, which relates to federal Schedule F, are posted to columns B and C.

19 Unemployment compensation. Unemployment compensation is not taxable on the California return, so the amount from federal Form 1040, line 19, is translated to column A and repeated at column B.

20a and 20b, Social security benefits and Taxable amount. Social security benefits are not taxable on the California return, so the amount from federal Form 1040, line 20b, is translated to column A, and column A is posted to column B.

21 Other income (federal). The total on federal Form 1040, line 21, is translated to column A. Adjustments to this total are separated into several parts, as follows.

21a California Lottery (column B). Enter any winnings from the California Lottery which were reported as income in line 21 of Form 1040. They are not taxable on the California return and will therefore be reported in column B.

21b Disaster loss carryover (column B). Disaster losses are no longer allowed except as carried over from the prior year's return. Enter only the carryover from a 2003 Form FTB 3805V (as a positive number).

21c NOL carryover in federal line 21 (column C). Enter here the entire net operating loss (NOL) deduction that was included in line 21 of the federal Form 1040. (The California NOL deduction is different from the federal NOL deduction, so the federal amount is added

back here and California amounts are deducted through lines 21d and 21e.)

21d NOL carryover from FTB 3805V (column B). Enter as a positive number the net operating loss (NOL) carryover from Part III, line 5 of California Form FTB 3805V.

21e NOL from FTB 3805Z/3806/3807 (column B). The NOL deductions from various special properties (Enterprise Zone and Program Area property, Los Angeles Revitalization Zone property, etc.) are claimed here. Enter as a positive number the NOL deduction from Forms FTB 3805D, FTB 3805Z line 4b, FTB 3806 line 2b, FTB 3807 line 4b, and FTB 3809 line 3b.

21f Other (describe). (*Supported by the California Adjustments Worksheet.*) Other additions or subtractions must be entered in the worksheets that support this line, with the sole exception of amounts from Form 3803, which are posted automatically. See FTB instructions for information on what else qualifies. The total additions and subtractions are summed from the worksheets to columns B and C. You must complete a separate worksheet for each separate item, describing each item in just 15 characters so that they appear on the printout as desired by the FTB. (CAUTION: If any of the adjustments entered here involve passive activities, you may also need to use the Passive Loss Worksheets on Form 3801 to report adjustments to passive activity gains and losses for lines 1 and 2 of Form 3801.) Note that reparation payments for forced or slave labor during World War II are not taxable on the California return, and should therefore be entered as a subtraction here if they were taxable on the federal return.

Subtractions/Additions from Form 3803. (*Road Map lines, supported by Form 3803*) If you elect to report your children's income on your own return, the income after the first \$1,600 is included in line 21 of federal Form 1040. Any California adjustments to this amount are posted here from the fifteen copies of Form 3803 that are built into the software (for reporting income from up to fifteen children).

Total other subtractions/additions. (*auto-calc lines.*) Computed as the adjustment totals from the above worksheets and Form 3803.

22 TOTAL. (*auto-calc lines*) Summed separately in columns B and C as the sum of lines 7 through 21f.

Section B -- Adjustments to Income. The second section corresponds to the adjustments section of Form 1040. California now conforms fully with federal law for the amounts on most lines in these section, so the corresponding amounts are taken directly from Form 1040 and posted to column A. Columns B and C do not appear for these lines because they can never have an amount on these lines. However, several lines can be different under California law, as highlighted below.

23 Educator expenses. California does *not* allow a deduction for educator expenses, so this amount will appear in column B as well as column A of the printed Schedule CA.

24 Certain business expenses of reservists, performing artists, and fee-basis government officials. You must generally refigure the amount to enter here under California law. As a result, this amount will appear in column B as well as column A of the printed Schedule CA, and you must enter any allowed deduction below.

C – Business expense addition. Enter here any amount on federal Form 2106 that is allowed under California law.

25 IRA deduction. Same as federal law.

26 Student loan interest deduction. California has not conformed with the new federal law that removes the restriction on the deduction to the first five years of the loan. You will therefore enter the disallowed amount on the next line.

Due past 5 years and other disallowance. California does not allow a deduction for voluntary payments nor interest scheduled to be paid AFTER the first 60 months (5 years) of the loan. In addition, the phaseout of the deduction as income increases starts at a lower level for California (\$60,000 vs. \$100,000 for married filing jointly and \$40,000 vs. \$50,000 for all others), so you may need to complete the Student Loan Interest Deduction Worksheet (in the FTB Instructions for Schedule CA) to determine the amount to enter here.

27 Tuition and fees deduction. California does *not* allow a deduction for higher education expenses, so this amount will appear in column B as well as column A of the printed Schedule CA.

28 Health savings account deduction. California does *not* allow this deduction, so this amount will appear in column B as well as column A of the printed Schedule CA.

29 Moving expenses. Same as federal law.

30 One-half of self-employment tax. Same as federal law.

31 Self-employed health insurance deduction. Same as federal law with one exception: California treats a registered domestic partner as your spouse. As a result, you may have an adjustment for column B or C if you have a registered domestic partner. See IRS instructions for details.

32 Self-employed SEP, SIMPLE, qualified plans. Same as federal law.

33 Penalty on early withdrawal of savings. Same as federal law.

34a Alimony paid. The amount in column A is translated from the corresponding line on the federal Form 1040. The SSN of the recipient is also translated, but you must enter the last name of the recipient as well for the California return. California law generally conforms to federal law, but if you are a nonresident alien and did not deduct alimony on the federal return, enter the amount in column C, since it is allowed on the California return.

Other adjustment in 1040 line 35. This amount, translated from the federal return, is the amount included in line 35 of federal Form 1040, but not in lines 23 through 34. It includes certain employee expenses from federal Form 2106, foreign housing deductions from federal Form 2555, plus any other amounts shown or itemized on the lines above line 35 of Form 1040.

If different for California, itemize. If the preceding amount is improper for the California return, you must report the difference in a supporting statement for this line. Be sure to enter the appropriate positive or negative adjustment to the preceding amount in the amount column of the supporting statement. The negative or positive adjustment is then reflected in column B or C for this line. *For example, California has not conformed with the Clean Air Fuel deduction, so you must report it as a negative amount in a supporting statement for this line.*

35 Add lines 23 through 34a. *(auto-calc lines)* Summed separately in columns B and C as the sum of lines 23 through 34a plus the preceding itemized adjustment.

The required posting of adjustments to Form 540 is determined in the remainder of this section:

36 TOTAL. *(auto-calc lines)* Line 35 is subtracted from line 22 separately in columns A, B and C. Column A is federal AGI, and columns B and C are California adjustments to federal AGI.

1040 line 36 on Form 540 line 13. *(auto-calc)* This is the AGI translated from the federal return to line 13 of Form 540. It should agree with the preceding amount computed for line 36, column A.

DISCREPANCY between Schedule CA and Form 540. *(auto-calc)* An amount will appear here if the federal AGI you reported on Form 540 differs from the federal AGI you reported on Schedule CA. *Any discrepancy here must be eliminated for a valid return.* Since all amounts in column of A of Schedule CA are translated from the federal return automatically, there should not be any discrepancy (unless you manually adjusted an entry due to changes you made in the federal return after translating it to the California return and failed to make the same adjustments on Form 540 and Schedule CA).

B-Total subtractions. *(auto-calc)* This is line 36, column B, computed as line 22, column B, less line 33, column B, this result could be negative if there is a greater subtraction for Section B (Adjustments to Income) than there is for Section A (Income).

C-Total additions. *(auto-calc)* This is line 36, column C, computed as line 22, column C, less line 33, column C, this result could be negative if there is a greater addition for Section B (Adjustments to Income) than there is for Section A (Income).

Subtraction for Form 540, line 14. *(auto-calc)* Computed as line 34B less line 34C, but no less than zero. This and the following compu-

tation ensure that amounts on the two adjustment lines of Form 540 are never negative.

Addition for Form 540, line 16. *(auto-calc)* Computed as line 34C less line 34B, but no less than zero.

Passive vs. Nonpassive adjustments. *(auto-calc)* Adjustments for all passive activities are summarized here. They are posted here from Worksheets C, E, and F, and Schedules D and D-1, whether or not they are reported on Form 3801. (Form 3801 is required by the FTB only when passive activities with losses are reported on the return. The automation of the return, however, requires a knowledge of all passive amounts whether or not Form 3801 is filed.) The result of this section is the "Total California nonpassive adjustment," which is the nonpassive part of line 22 of Schedule CA. This result is provided for information only, and is not used directly in the return.

PART II, ADJUSTMENTS TO FEDERAL ITEMIZED DEDUCTIONS. The second part collects all differences from federal Schedule A.

37 Federal itemized deductions. *(Road Map line, supported by Worksheet A.)* Total federal itemized deductions BEFORE limitation for high incomes is posted here from Worksheet A.

38 State, local, SDI, and foreign income taxes. *(Road Map line, supported by Worksheet A.)* Only adjustments for income taxes deducted on the federal return are posted here from Worksheet A.

39 Subtract line 38 from line 37. *(auto-calc)* Computed as indicated.

40 Other adjustments (Worksheet A). *(Road Map line, supported by Worksheet A.)* All adjustments from Worksheet A not posted to line 38, above, are posted here. This includes depreciation and passive activity adjustments that are relevant to federal Schedule A alone.

Specify for line 40. If an amount appears above from Worksheet A, this entry is automatically "See Worksheet A" so that the FTB will know where to look for details. However, if you decide not to send Schedule A, you must remove it from the return with our File Manager (Chapter 9 of the User's Guide) then return to this line and enter your own explanation on this line or a supporting statement for it. *CAUTION: For an e-file return you MUST explain any amount on line 40 in a supporting statement for this line because our Worksheet A is not accepted as support for e-file.* (You must use the F10 key to access the support here because this is a text entry line.)

41 Combine line 39 and line 40. *(auto-calc)* Computed as the sum of lines 40 and 41.

Federal AGI on Form 540, line 13. *(auto-calc)* Taken from Form 540 as indicated.

Schedule A line 4, 13, 19, and gambling. *(Road Map line, supported by Worksheet A.)* The part of itemized deductions NOT subject to the high income limitations is posted here from Worksheet A. The amount posted here is the California-adjusted version of the federal amounts cited.

Part of line 41 disallowed. *(auto-calc)* Computed from the preceding three lines using the FTB Itemized Deductions Worksheet.

42 California itemized deductions. *(auto-calc)* Computed as line 41 less the above disallowed amount.

Standard deduction. *(auto-calc)* The standard deduction for your filing status appears here automatically (\$3,070 or \$6,140 for 2004).

43 Larger of line 42 or standard deduction. *(auto-calc)* Computed as indicated.

The result on line 43 is posted to Form 540, line 18.

Extra line for personal memos. Provided for supporting statements that will not be printed with the official return.

Schedule D / Capital Gain or Loss Adjustment

Conformity in the law, but not the form. California law conforms closely to federal law in the reporting of capital gains and losses, but details of the forms are glaringly different. Nevertheless, you can refer to the section for Schedule D in Chapter 2 of the regular Tax Forms Guide 2005 Edition for many details. However, California has defined a different procedure than the IRS for reporting sec. 1202 exclusions (sec. 18152.5 of the California code). In addition, California does not provide favorable taxation for long-term capital gains, so the California schedule does not have separate sections for long-term and short-term transactions. Moreover, California has separate columns for gains and losses, unlike the federal Schedule D where only net results are shown. As a result, translation of amounts from the federal Schedule D is not always straightforward.

Translation from the federal return is complete ... ALMOST. As far as the net gain or loss on Schedule D is concerned, the translation from the federal return automatically produces the proper bottom line as long as there are no adjustments for basis or carryovers from prior years, and no difference in the sec. 1202 exclusion claimed. Lines 1, 2, and 3, and their supporting worksheets, are translated automatically from the federal return. As far as *computations* are concerned you need make entries only if

- there is a capital loss carryover from the 2003 California Schedule D, which you must enter on line 6, or
- you claimed a section 1202 exclusion on federal Schedule D, and the exclusion for the corresponding California section 18152.5 is not allowed because 80% of the corporations employment and spending is not in California, or
- some items reported on the translated worksheets, or other forms that support line 1, have a different basis under California rules (which is likely if you claimed depreciation before 1987 for the sold property, you claimed bonus depreciation or section 179 expenses in recent years, or you claimed Special California Credits that require you to reduce the basis by the amount of the credit).

However, even if none of the above apply, extra effort must be taken in preparing the California Schedule D in order to conform with its different format.

MANDATORY extra steps: You must view all Gain/Loss Worksheets after their translation from the federal return. Since 1997, the federal Schedule D does not separately show gains and losses. Therefore, when we translate the federal worksheets, no amounts are translated to the separate loss and gain lines of the California worksheets (columns d and e on the California Schedule D). As a result, you must view all California worksheets after they are translated in order for the separate losses and gains to show up on the worksheet and on the printouts for line 1. (Unlike forms, worksheets recalculate whenever you view them, so the mere access to a worksheet is enough to cause the gain and loss lines to calculate to their proper amounts. The computed re-

sults for the schedule are correct even if you don't view the worksheets because the software merely assigns a net loss to the loss column and a net gain to the gain column, ensuring the proper mathematics in the final net result.)

Itemized sales for line 1a. Line 1a is a catch-all for all short-term and long-term gains and losses on the federal Schedule D, except for those reported to you on a Schedule K-1 (form partnerships, etc.).

Amounts supported by worksheets on the federal Schedule D. The first set of lines are translated from the worksheets that support lines 1 and 8 of the federal Schedule D:

ST net gain or loss. (*Supported by Gain/Loss Worksheets*) The net gain or loss from federal Schedule D, line 1 appears here. Remember to view the translated worksheets that are attached to this line to ensure that gains and losses appear in the separate gain and loss columns of the California Schedule D.

ST capital sales (d) loss. (*auto-calc, supported by Gain/Loss Worksheets*) Once you view the worksheets, the sum of losses on those worksheets appears on this line. Until then, any loss seen on the above net line appears here as a positive amount.

ST capital sales (e) gain. (*auto-calc, supported by Gain/Loss Worksheets*) Once you view the worksheets, the sum of gains on those worksheets appears on this line. Until then, any gain seen on the above net line appears here as a positive amount.

LT net gain or loss. (*Supported by Gain/Loss Worksheets*) The net gain or loss from federal Schedule D, line 8 appears here. Remember to view the translated worksheets that are attached to this line to ensure that gains and losses appear in the separate gain and loss columns of the California Schedule D.

LT capital sales (d) loss. (*auto-calc, supported by Gain/Loss Worksheets*) Once you view the worksheets, the sum of losses on those worksheets appears on this line. Until then, any loss seen on the above net line appears here as a positive amount.

LT capital sales (e) gain. (*auto-calc, supported by Gain/Loss Worksheets*) Once you view the worksheets, the sum of gains on those worksheets appears on this line. Until then, any gain seen on the above net line appears here as a positive amount.

Amounts supported by forms on the federal Schedule D. The next set of lines show amounts that are *not* reported on worksheets for the federal Schedule D, but are reported on separate federal forms, with only the totals shown on the federal Schedule D (lines 4 and 11). However, *California requires that all of these amounts be reported in the chart for line 1a, so they must be reported on our worksheets for line 1a.* We have therefore devised a semi-automatic procedure for accomplishing this task. In the following lines, all amounts either translated from components of lines 4 and 11 of the federal Schedule D or transferred from separate California

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forms. To get these amounts onto worksheets, as the FTB requires, you must itemize the worksheet line that follows the totals for a particular form. However, you do not enter anything on the worksheet you access; you merely view them then exit. They are completed automatically for you based on the totals, with the proper description that applies:

Business property gain (Schedule D-1). (*Road Map line, supported by Schedule D-1.*) The long-term gain in Part I of Schedule D-1 appears here, analogous to the federal Form 4797 amount that contributes to line 11 of federal Schedule D.

Schedule D-1 amount for line 1a. (*Supported by Gain/Loss Worksheets*)

If an amount appears on the preceding line you MUST itemize this line in order for the amount to be properly reported in the FTB chart for line 1a. Once you see the amount on the worksheet you can return here and proceed to the next line.

Installment sales gain (Form 3805E). (*Road Map line, supported by Form 3805E.*) The gain from Form 3805E appears here, analogous to the federal Form 6252 amounts that contribute to lines 4 and 11 of federal Schedule D.

FTB 3805E amount for line 1a. (*Supported by Gain/Loss Worksheets*)

If an amount appears on the preceding line you MUST itemize this line in order for the amount to be properly reported in the FTB chart for line 1a. Once you see the amount on the worksheet you can return here and proceed to the next line.

** **Itemizing discrepancy above.** (*auto-calc*) If an amount appears on this line it means that you have failed to itemize to the supporting worksheets above when required. You must return to the preceding lines and itemize the worksheet line that follows a non-zero amount.

Casualty net (Form 4684) in Federal Schedule D, line 4. The short-term gain or loss on Form 4684 that was included in line 4 of federal Schedule D is translated here from the federal return.

Casualty net (Form 4684) in Federal Schedule D, line 11. The long-term gain or loss on Form 4684 that was included in line 11 of federal Schedule D is translated here from the federal return.

Form 4684 amount for line 1a. (*Supported by Gain/Loss Worksheets*) If an amount appears on either of the preceding two lines you MUST itemize this line in order for the amounts to be properly reported in the FTB chart for line 1a. Once you see the amount on the worksheet you can return here and proceed to the next line.

Section 1256 net (Form 6781) in Federal Schedule D, line 4. The short-term gain or loss on Form 6781 that was included in line 4 of federal Schedule D is translated here from the federal return.

Section 1256 net (Form 6781) in Federal Schedule D, line 11. The long-term gain or loss on Form 6781 that was included in line 11 of federal Schedule D is translated here from the federal return.

Form 6781 amount for line 1a. (*Supported by Gain/Loss Worksheets*) If an amount appears on either of the preceding two lines you MUST itemize this line in order for the amounts to be properly reported in the FTB chart for line 1a. Once you see the amount on the worksheet you can return here and proceed to the next line.

Like-kind exchange net (Form 8824) in Federal Schedule D, line 4. The short-term gain or loss on Form 8824 that was included in line 4 of federal Schedule D is translated here from the federal return.

Like-kind exchange net (Form 8824) in Federal Schedule D, line 11. The long-term gain or loss on Form 8824 that was included in line 11 of federal Schedule D is translated here from the federal return.

Form 8824 amount for line 1a. (*Supported by Gain/Loss Worksheets*) If an amount appears on either of the preceding two lines you MUST itemize this line in order for the amounts to be properly reported in the FTB chart for line 1a. Once you see the amount on the worksheet you can return here and proceed to the next line.

RIC or REIT gain (Form 2439) in Federal Schedule D, line 11. The long-term gain on Form 2439 that was included in line 11 of federal Schedule D is translated here from the federal return.

Form 2439 amount for line 1a. (*Supported by Gain/Loss Worksheets*) If an amount appears on either of the preceding two lines you MUST itemize this line in order for the amounts to be properly reported in the FTB chart for line 1a. Once you see the amount on the worksheet you can return here and proceed to the next line.

**** Itemizing discrepancy above.** (*auto-calc*) If an amount appears on this line it means that you have failed to itemize to the supporting worksheets above when required (on the current screen). You must return to the preceding lines and itemize the worksheet line that follows a non-zero amount.

1b Sec. 18152.5 exclusion. This line is the FTB's answer to the federal Section 1202 exclusion. For stocks that qualify the rules are the same for California: up to 50% of qualifying sec. 1202 gain can be excluded from income on your return. However, to qualify for California exclusion the corporation issuing the stock must have 80% of its employment and spending in California. Consequently, some of the exclusion claimed on the federal return may not be available for the California return.

1b Net sec. 18152.5 exclusion. (*Supported by Sec. 18152.5 Gain Worksheet, Figure CA-2.*) The worksheet for this line is preformatted to implement the reporting format defined by the FTB for sec. 18152.5 exclusions. Unfortunately, the FTB-defined format is not the same as the IRS-defined format, so to fully comply with the FTB instructions you will have to remove the worksheets translated to line 1a for sec. 1202 transactions, and reenter all their data here instead. Moreover, the FTB wants all sec. 1202 transactions combined so that line 1b shows the combined result of the exclusion or

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adjustment to be reported, with column (a) showing only "Section 18152.5 exclusion." You are therefore not allowed to create more than one worksheet for this line. As explained when the worksheet is described, later, the result of the worksheet is the total sec. 1202 exclusions allowed by California law in column (d) and the total sec. 1202 gain before exclusion in column (e).

(d) California exclusion. *(auto-calc)* This is the amount on line d of the above worksheet, and is the total sec. 1202 exclusions allowed by California law.

(e) Entire gain. *(auto-calc)* This is the total of all sec. 1202 gain before exclusion.

| SEC 18152.5 GAIN | SECTION 18152.5 EXCLUSION |
|--|---------------------------|
| a. Description | |
| For Capital Gain Dist'ns: | |
| Section 1202 gain in CGD... | 0 |
| Amt qlfd for Cal exclusion | 0 |
| For other than CGD: | |
| If more than one date, bypass date checking & enter VARIOUS. | |
| Bypass date checking...? No | |
| Date acquired(mm/dd/yy) | |
| Date sold (mm/dd/yy) | |
| b. Sales price | 0 |
| c. Cost or other basis... | 0 |
| NET (your entry if b=c=0). | 0 |
| Amt qlfd for Cal exclusion | 0 |
| Summary: | |
| d. Loss | 0 |
| e. Gain | 0 |

Figure CA-2. Section 18152.5 Gain Worksheet

to achieve a valid computation of the return, its use is required to comply strictly with the FTB format for this reporting. However, *if you choose to comply with the FTB format by using this worksheet, you MUST not only complete this worksheet but also remove from line 1a any worksheets related to sec. 1202 gains.*

a. Description. *(auto-calc)* This line is automatically "Section 18152.5 exclusion," as required by the FTB.

For Capital Gain Distributions. Once you view this worksheet, any section 1202 gain from box 2d of Form 1099-DIV that is included in line 3 of Schedule D is automatically removed from that line, as the FTB prefers. You must then identify on this worksheet the amount that qualifies for exclusion, and the rest is automatic.

Section 1202 gain in CGD. *(auto-calc)* This is the total of all sec. 1202 gains before exclusion that are shown above line 3 of Sch. D. This amount will be included in line e, below.

Amount qualified for California exclusion. Enter the amount to exclude on the California return, which is up to 50% of the preceding amount. This amount will be included in line d, below.

For other than CGD. The remaining entries relate to all other sec. 1202 gains, and must be removed from the worksheets for line 1a. If you have more than one sec. 1202 gain to report, you enter Yes for "Bypass date checking?" and skip the dates, sales price, and cost entries, and use only the NET entry described below.

Bypass date checking? A Yes here allows you to omit the following date entries.

Dates acquired and sold. You should enter dates only if you are reporting only one sale on this worksheet.

b. Sales price. You should enter the sales price only if you are reporting only one sale on this worksheet.

c. Cost or other basis. You should enter the basis only if you are reporting only one sale on this worksheet.

NET (your entry if $b=c=0$). If you made no entries on b and c, enter here the full sec. 1202 gain reported on the federal return, before applying any exclusions. If you did make an entry on line b or c, the net gain will appear here automatically. This amount will be included in line e, below.

Amount qualified for California exclusion. Enter the amount to exclude on the California return, which is up to 50% of the preceding amount. This amount will be included in line d, below.

Summary:

d. Loss. *(auto-calc)* Computed as the sum of two lines above for amount qualified for California exclusion.

e. Gain. *(auto-calc)* Computed as the sum of sec. 1202 gain in CGD and the NET gain above.

1a and 1b combined. *(auto-calc lines)* All gains and losses are separately summed for all of the preceding lines and the total is shown here. This is the net amount reported in the chart for line 1 of California Schedule D.

K-1 gains and losses for line 2. Line 2 is designed for gains and losses reported to you on a Schedule K-1, from partnerships, S corporations, fiduciaries, and limited liability companies. The amount for this line is translated from the worksheets that support lines 5 and 12 of the federal Schedule D. However, you should note that amounts reported to you by partnerships and fiduciaries may be different for the state return, so you must carefully read the Schedules K-1 you receive from them.

ST net gain or loss on K-1. *(Supported by Sch. K-1 Gain/Loss Worksheets)* The net gain or loss from federal Schedule D, line 5 appears here. Remember to view the translated worksheets that are attached to this line to ensure that gains and losses appear in the separate gain and loss columns of the California Schedule D.

ST partnership/S-corp/fiduciary (d) loss. *(auto-calc, supported by Sch. K-1 Gain/Loss Worksheets)* Once you view the worksheets, the sum of losses on those worksheets appears on this line. Until then, any loss seen on the above net line appears here as a positive amount.

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ST partnership/S-corp/fiduciary (e) gain. (*auto-calc, supported by Sch. K-1 Gain/Loss Worksheets*) Once you view the worksheets, the sum of gains on those worksheets appears on this line. Until then, any gain seen on the above net line appears here as a positive amount.

LT net gain or loss on K-1. (*Supported by Sch. K-1 Gain/Loss Worksheets*) The net gain or loss from federal Schedule D, line 12 appears here. Remember to view the translated worksheets that are attached to this line to ensure that gains and losses appear in the separate gain and loss columns of the California Schedule D.

LT partnership/S-corp/fiduciary (d) loss. (*auto-calc, supported by Sch. K-1 Gain/Loss Worksheets*) Once you view the worksheets, the sum of losses on those worksheets appears on this line. Until then, any loss seen on the above net line appears here as a positive amount.

LT partnership/S-corp/fiduciary (e) gain. (*auto-calc, supported by Sch. K-1 Gain/Loss Worksheets*) Once you view the worksheets, the sum of gains on those worksheets appears on this line. Until then, any gain seen on the above net line appears here as a positive amount.

2 Net shown on K-1s, (d) loss and (e) gain. (*auto-calc lines*) Computed separately for column (d) and (e), this is the sum from all short-term and long-term worksheets for this line.

Passive Activity Details. The rules for passive activity losses are the same for California returns as they are for federal returns, so Form 3801 is handled just like federal Form 8582. (See FTB instructions for special rules on the sale of California small business stock and California basis determination.) Loss amounts are automatically reduced by any proportionate disallowances from Form 3801. You should refer to the regular Tax Forms Guide 2005 Edition for details. CAUTION: In order for the amounts on the worksheets to reflect the proper disallowances from Form 3801, you must view all worksheets after the final recalculation of the return to ensure that they are updated with the proper prorated share of disallowed losses. Otherwise the amounts printed in the chart for line 1 may disagree with the total losses seen in line 4 of this schedule.

3 Capital gain distributions. All amounts in this section are translated from the federal return, but the reporting format defined by the FTB differs from that defined by the IRS. Whereas the IRS instructs you to include ALL capital gains distributions on line 13 of federal Schedule D (box 2a of Forms 1099-DIV), the FTB instructs you to exclude the part identified in box 2d of Forms 1099-DIV as section 1202 gain. However, if you view the California Schedule D before accessing the Sec. 18152.5 Gain Worksheet, line 3 will not yet have the sec. 1202 gain excluded. Nevertheless, the results for the return will still be valid if the exclusion taken on the federal return is valid for the California return. But as soon as you view the Sec. 18152.5 Worksheet, the sec. 1202 gain is removed from this line and any allowed exclusion must be entered on the worksheet.

Capital Gain Distributions on Form 3803. (*Road Map line, supported by Form 3803.*) The amount from Form 3803 for capital gain distributions distributed to the taxpayer's child is posted here.

Sec. 1202 part of the above. (*Road Map line, supported by Form 3803.*) The part of the above capital gain distribution that is sec. 1202 gain (as identified in box 2d of Forms 1099-DIV) appears here.

Other reportable Capital Gain Distributions. All other amounts included in line 13 of federal Schedule D are translated to this line, including any amounts on federal Schedule B.

Sec. 1202 part of the above. The part of the above capital gain distribution that is sec. 1202 gain (as identified in box 2d of Forms 1099-DIV) is translated to this line.

Total sec. 1202 gain in CGD. (*auto-calc*) Computed as the sum of the above two sec. 1202 gains.

Amount reported on 1b instead. (*auto-calc*) Once you create a Sec. 18152.5 Worksheet, the preceding total appears at line 1b, column (e), and is posted here so that it can be automatically removed from the total at line 3, below.

3 Capital gain distributions. (*auto-calc*) Computed as the sum of "Capital Gain Distributions on Form 3803" plus "Other reportable Capital Gain Distributions" less "Amount reported on 1b instead."

4 Total 2004 gains from all. (*auto-calc*) Computed as the sum of gains on all worksheets and lines above -- column (e) of Schedule D.

5 2004 loss. Add column d of lines 1 and 2. (*auto-calc*) Computed as the sum of losses on all worksheets and lines above -- column (d) of Schedule D -- less any passive loss disallowed from Form 3801.

6 California capital loss carryover from 2003, if any. Carryover for California will almost always be different from any carryover for a federal return because the laws have differed greatly in the past. *Consequently, no carryover amount is translated from the federal return.* You must enter the carryover here yourself based on prior California returns.

7 Total 2004 loss. Add lines 5 and 6. (*auto-calc*) Computed as indicated.

8 Combine line 4 and line 7. (*auto-calc*) Computed as line 4 less line 7, this is the net gain or loss before the annual limitation on loss deductions.

9 If line 8 is a loss, the smaller of line 8 and \$3,000 (\$1,500 if MFS). (*auto-calc*) Computed as indicated.

10 Amount from federal Form 1040, line 13. This entry is translated from federal Schedule D, which is posted to Form 1040, line 13, of the federal return.

11 California gain on 8 or loss on 9. (*auto-calc*) Computed as line 8 if a gain, or line 9 (as a negative amount) if line 8 is a loss. .

12 Adjustment (a) decrease or (b) increase for Schedule CA. (*auto-calc lines*) A net adjustment is computed as line 11 less line 10. If the result is less

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than zero it is shown as a positive number on line 12a and posted to line 13 column B of Schedule CA. If it is greater than zero it is shown on line 12b and posted to line 13 column C of Schedule CA.

Carryover to 2005. (*auto-calc lines*) Ordinarily, the carryover to 2005 is just the full loss on line 8 less the deductible amount on line 9. But if the deductible loss would make taxable income less than zero, a corresponding extra amount can be carried over to next year. The 8-line calculation that appears here, which follows the California Capital Loss Carryover Worksheet that appears in the FTB instructions for Schedule D, ensures the maximum allowed carryover.

Reconciliation with Form 3801. (*auto-calc lines*) The final lines show the passive part of the adjustment, which is needed for special AGI calculations on Form 3801. The line labeled "Negative of federal passive net" is computed from amounts translated from federal Schedule D, and will be the negative of the line that precedes it labeled "Total passive net on D" if there are no differences between federal and California amounts reported.

Schedule D-1 / Sales of Business Property

California law conforms well to federal law. Conformity between California Schedule D-1 and federal Form 4797 is complete as far as the law is concerned. You can therefore refer to the section on Form 4797 in Chapter 2 of the regular Tax Forms Guide 2005 Edition for most details. In addition, for the first time in years, the California Schedule D-1 follows the same format as federal Form 4797, eliminating the former omission of lines for like-kind exchanges and the former separate columns for gains and losses.

Translation from the federal return is virtually complete. Because California now conforms to the federal format, the translation from the federal return automatically produces the proper bottom line as long as there are no adjustments for basis. As a result, you need to make adjustments to translated amounts only if

- some items reported on the translated worksheets or other forms that support Form 4797 have a different basis under California rules, which is likely if you claimed depreciation before 1987 for the sold property or you claimed Special California Credits that require you to reduce the basis by the amount of the credit, or
- you are reporting sales of Section 1250 or 1254 property in Part III of Schedule D-1, for which California lagged changes in federal law by one year. (Dates for certain lines are one year later on the California return than they are on the federal return, for pre-1977 events).

Except for the above adjustments, you need not view the Gain/Loss Worksheets for the California Schedule D-1 in order for the schedule to compute the proper gains and losses.

*Schedule G-1 / Tax on Lump-Sum Distributions

Purpose. This form, which is analogous to Federal Form 4972, is used to take advantage of a special tax break for total distributions from qualified plans.

*** Included in Premium Level software ONLY.** This form is only built into the Premium Level version of the California Supplement. It is detailed in the separate *Premium Level Supplement 2005*. (When available, Schedule G-1 is accessible through the Road Map at line 23 of Form 540.)

Schedule P / Alternative Minimum Tax and Credit Limitations

Purpose. Schedule P serves two purposes: to compute the alternative minimum tax (Parts I and II, on page 1) and to consolidate and limit credits (Part III, on page 2). Both pages of the schedule are automatically created when needed, based on separate requirements. Schedule P, page 1 is automatically created and completed upon the final recalculation of the return when you are liable for the alternative minimum tax (unless you specified the blocking of its auto-creation through the question on the Control Form). (The determination to create the form is made independently of the federal return because it is possible to be liable for the California minimum tax even though a federal Form 6251 was not required.) Unless further modified by page 2 of Schedule P, the result on line 26 is automatically posted to line 35 of Form 540. Schedule P, page 1 is also automatically created when Schedule P, page 2 exists, and Schedule P, page 2 is created when a credit that is subject to limitation through Schedule P is claimed.

PARTS I and II - ALTERNATIVE MINIMUM TAX. Page 1 of Schedule P no longer closely parallels federal Form 6251 because the IRS redesigned Form 6251 for 2002 and the FTB has not conformed to the new design. However, differences between California and federal law are similar to the past:

- Federal Form 6251 has no equivalent for the preference at line 13a of California Schedule P, Appreciated contributions.
- California Schedule P has no equivalent for the preference at line 15 of federal Form 6251, Electing large partnerships.
- The preference at line 13l of Schedule P, which is analogous to line 12 of Form 6251, is 50% of the sec. 18152.5 exclusion taken on California Schedule D rather than 7% of the sec. 1202 exclusion taken on federal Schedule D. This difference is automatically reflected in Schedule P once California Schedule D is completed.
- Federal Form 6251 has no equivalent for the AMTI exclusion at line 17 of Schedule P, which is detailed next.
- The thresholds for phaseout of itemized deductions at line 18 and the exemption amount at line 22 are different from the federal counterparts, but the computational methods are identical. *(Note that the federal equivalent of Sch. P, line 18 no longer appears on Form 6251, but is instead reflected in the computation for line 1. The federal equivalent of Sch. P, line 22 is Form 6251, line 29.)*
- The computation of the alternative minimum tax is more complex for federal Form 6251 than California Schedule P because of the 2-tier percentages used and the special computations required because of the reduced capital gains tax on the federal return.

Except for these items, you can refer to the section on Form 6251 in Chapter 2 of the regular Tax Forms Guide 2005 Edition for most details. This part of Schedule P is already complete for many taxpayers as a result of the soft-

ware's translation from the federal return to the California return. Adjustments for differences in itemized deductions and the standard deduction are automatic as well. You may have to change some entries, however, to reflect remaining differences, especially if you have any ownership interest in a trade or business. You should take particular care to read the FTB instructions for Schedule P if you have any entries for lines 7 (Investment interest expense), 8 (Post-1986 depreciation), 9 (Adjusted gain or loss), 13a (Appreciated contributions), 13d (Depreciation pre-1987), 13e (Installment sales), or 13g (Long-term contracts). The amounts automatically translated from the federal return will often not be the same as the proper California amounts. *CAUTION: The federal 30% and 50% special allowance for first-year depreciation carries with it a forgiveness of the tax preference of accelerated depreciation for the property. Therefore, since California has not conformed with the special allowance, you must you generally make an adjustment at line 8 of Schedule P for new tangible property even when you have no such adjustment on the analogous line 17 of federal Form 6251.*

Exclusion for small businesses. California has a special exclusion for some taxpayers, for which there is no federal equivalent. If the taxpayer's gross income from all trades or businesses combined is less than \$1 million, no amounts related to those trades or businesses is to be used on Schedule P in computing the alternative minimum tax. If you qualify, you should enter no adjustments or preferences related to those trades or businesses in Part I of Schedule P. The software will remove the taxable income from those trades or businesses, if the aggregate net is greater than zero, at line 17 in Part I of Schedule P, as follows:

Gross income on California C, E, F. *(auto-calc)* Taken from the worksheets built into the software for figuring adjustments to federal Schedules C, E, and F. The three amounts posted here are: gross income on line 1 of Worksheet C, partnership/S Corp self-employment gross on Worksheet E, and gross income on line 1 of Worksheet F.

Sales on Sch. D-1 lines 2 and 10. *(auto-calc)* Taken from Schedule D-1 as indicated.

Other sales on Sch. D-1. Since the above amounts reflect ONLY the sales entered in the gain/loss worksheets for lines 2 and 10, and do NOT include gross receipts for partnerships or for sales reported in Part III of Schedule D-1, you must enter the gross sales for these other items here.

Other trade or business gross income. Enter here all gross income from trades or businesses not included in the above lines. For the purposes of the AMTI exclusion, gross income is gross receipts less returns and allowances for all trades and businesses you own (or your proportional share for trades and businesses in which you have an ownership interest).

Aggregate gross income. *(auto-calc)* Computed as the sum of the above four amounts of gross income.

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Net income on California C, E, F. *(auto-calc)* Taken from the worksheets built into the software for figuring adjustments to federal Schedules C, E, and F. The three amounts posted here are: California net profit or loss on line 5 of Worksheet C, partnership/S Corp self-employment net on Worksheet E, and California net profit or loss on line 5 of Worksheet F.

Net on Sch. D-1 line 7 or 9, and line 18(b)(2). *(auto-calc)* Taken from Schedule D-1, this total includes both the long-term capital gains that are posted to Schedule D and the ordinary gains retained on Schedule D-1.

Other trade or business net income. Enter here all net taxable income from trades or businesses not included in the above lines (or your proportional share for trades and businesses in which you have an ownership interest).

Aggregate taxable income. *(auto-calc)* Computed as the sum of the above three amounts of net income.

Qualified for AMTI exclusion. *(auto-calc)* Automatically Yes if the "Aggregate gross income" is under \$1,000,000, and No otherwise.

17 AMTI exclusion. *(auto-calc)* Computed as the "Aggregate taxable income" if the above answer is Yes, and zero otherwise.

CAUTION: For a consistent return, if the answer to "Qualified for AMTI exclusion" is Yes, you must remember to OMIT from your entries in Part I of Schedule P any adjustments or preferences related to any trades or businesses included above.

Itemize for Parts III (Credits). *(Road Map line.)* This line provides direct access to the remainder of Schedule P, which is page 2 of the schedule. The schedule is split in the software because of its unusually high length. The remainder of the schedule is therefore accessed as a separate form even though it calculates and prints as a continuation of Schedule P, page 1.

PART III - CREDITS THAT REDUCE TAX. Part III of this schedule is used to consolidate tax credits and limit them in a systematic way to remaining tax balances. In addition, some of the credits are further limited when a tentative minimum tax (line 24 of Schedule P, page 1) or an alternative minimum tax (line 26 of Schedule P, page 1) exists. There is no federal equivalent to this page of the schedule, and the California rules for most credits differ substantially from the federal rules.

1 Amount from Form 540, line 24. *(auto-calc)* Computed as line 24 of Form 540 refigured using the exemption credits on line 5, above.

2 Tentative minimum tax from Part II, line 24. *(auto-calc)* Taken from line 24 of Schedule P, page 1.

3 Subtract line 2 from line 1. *(auto-calc)* Computed as indicated, but no less than zero, this is "excess tax" -- the amount by which the tax before credits on Form 540 exceeds the tentative minimum tax on Schedule P page 1.

Line 3 is the tax balance that may be offset by credits in Section A.

SECTION A - CREDITS THAT REDUCE EXCESS TAX. The current-year claims for the credits in this section are not allowed to exceed line 3, above, in the aggregate. That is, they cannot reduce tax to any less than the amount of tentative minimum tax.

A1 Credits that reduce excess tax and have no carryover provisions. The credits in this section can be used ONLY in the current year. Any amount of credit not allowed this year for these credits cannot be carried over to any other year. Each credit is therefore printed on the official Schedule P in a 3-column format as follows, even though not all lines are shown on the screen for all credits.

Total credit amount (column a). The gross (tentative) credit is entered or calculated on the numbered line that describes the credit, and is printed in column (a) of the official Schedule P.

Credit used this year (column b). (auto-calc) Computed as the lesser of the preceding total credit amount (column a) and the tax balance that exists in column (c) before this credit is applied. This entry is printed in column (b) of the official Schedule P.

Tax Balance. (auto-calc, not shown on the screen) Computed as the tax balance after subtracting the above credit used this year, column (b), from the tax balance in column (c) of the previous allowed credit. This entry is printed in column (c) of the official Schedule P. Subsequent credits are limited to this amount.

All credits on lines 4, 5, and 6 follow the above printed format, and the computation of the last two lines, above, is identical in every case (and so these two lines are not detailed below for these credits). However, the data entry required varies, as follows:

4 Code 214, Long-term care. You may claim \$500 for each qualifying person by filing Form 3504 (*built into the software for the Premium Level*) with the return, entering the result from that form here.

5 Code 162, Prison inmate labor credit. You may claim a credit for as much as 10% of the wages paid to prison inmates under a qualifying plan. You must file Form 3507 (not built into the software) with the return, and enter the result from that form here.

6 Code 169, Enterprise zone employee credit. You must file Form 3553 (*built into the software for the Premium Level*) with the return, and enter the result from that form here.

A2 Credits that reduce excess tax and have carryover provisions. Unused credits on these lines can be carried over to the next year. And for some of them the carryover can even be used in section B2 first, where they may be allowed in the current year. Internally, the computation of current-year amounts and carryovers involves the following four lines, even though typically only the first two lines appear on the screen.

Total credit amount. The gross (tentative) credit is entered on, calculated at, or posted from Form 3540 to the line that describes the credit, and is printed in column (a) of the official Schedule P at line 12, 13, 14, or 15, described later.

Schedule P

Credit used this year. *(auto-calc)* Computed as the lesser of the preceding total credit amount and the tax balance that exists before this credit is applied. This entry is printed in column (b) of the official Schedule P at line 7, 8, 9, or 10, described later.

Tax balance. *(auto-calc)* Computed as the tax balance after subtracting the above credit used this year from the tax balance of the previous allowed credit. This entry is printed in column (c) of the official Schedule P at line 7, 8, 9, or 10, described later.

Credit carryover. *(auto-calc)* Computed as the total credit amount less the credit used this year. This is the amount that can be claimed next year, or, in some cases, carried over to Section B2, and is printed in column (d) of the official Schedule P at line 7, 8, 9, or 10, described later.

All of the following credits follow the above format, and all auto-calc lines are computed the same, so only the lines for the total credit amounts are detailed in the following.

Order of credits arranged for maximum credit this year. With the major redesign by the FTB of this part of Schedule P, the order for claiming credits is no longer set by the design of the form for most credits. For credits not specifically listed on the official preprinted FTB form, the taxpayer is now free to claim the credits in any order. As a result, we have chosen, in designing the software, the order that maximizes the amount that can be claimed in the current year. This means that credits that have the most severe limitations are claimed first, and those with the least severe limitations are claimed last. With this in mind, we have organized the credits for sections A2, B, and C into five groups, and ordered them from the most restricted group to the least restricted group. Within each group we have arranged the credits alphabetically (as they are in the current FTB instructions for Schedule P).

Current credits carried over to next year. The first group of credits is comprised of current credits (for 2004 expenses), and the amounts not used this year are carried over to next year:

Code 209, Community Development Financial Institution Investments.

You may claim as much as 20% of each qualified investment, but you must obtain certification from California Organized Investment Network (COIN), Department of Insurance, 300 Capitol Mall, Suite 1460, Sacramento, CA 95814.

Code 205, Disabled access. This credit is similar to the comparable federal credit, but is limited to \$125 or half of the qualified expenditures, whichever is less. You must complete FTB 3548 (*built into the software for the Premium Level*), and enter the result from that form here.

Code 204, Donated agricultural products transportation. This credit allows a credit up to 50% of the costs paid or incurred for the transporting of agricultural products donated to nonprofit charitable

organizations. You must complete FTB 3547 (not built into the software), and enter the result from that form here.

Employer child care. You must complete FTB 3501 (*built into the software only for the Premium Level*) and enter the appropriate amount for the next two credits:

Code 190, Employer child care contribution. 30% of your contributions to a qualified child care plan are reimbursed here as a credit. Enter the amount from the "child care contribution" portion FTB 3501.

Code 189, Employer child care program. The costs of establishing a child care program or constructing a childcare facility are reimbursed here as a credit. Enter the amount from the "child care program" portion FTB 3501.

Code 203, Enhanced oil recovery. This credit is similar to the comparable federal credit, but the credit is only one-third of the federal credit and is limited to qualified projects located within California, as figured on FTB 3546 (not built into the software).

Code 207, Farmworker Housing Construction. You may claim as much as 50% of qualified costs for new construction, but you must obtain certification from Farmworker Housing Assistance Program, California Tax Credit Allocation Committee, 915 Capitol Mall, Room 485, Sacramento, CA 95814.

Code 215, Joint Strike Fighter -- Wages. You may claim up to 50% of qualified wages up to \$10,000, as computed on form FTB 3534.

Code 216, Joint Strike Fighter -- Property. You may claim up to 10% of the cost of property to be used in a joint strike fighter, as computed on form FTB 3534.

Code 198, Local agency military base recovery (LAMBRA) hiring and sales and use tax. Enter here your business incentives for LAMBRAAs figured on FTB 3807 (not built into the software), which you must file with the return.

Code 211 Manufacturing Enhancement Area (MEA) Hiring. This credit is a percentage of qualified wages paid to the disadvantaged. It is claimed through FTB Form 3808 (not built into the software).

Code 206, Rice Straw. You may claim as much as \$15 per ton of purchased rice straw grown in California, but you must obtain certification from Rice Straw Tax Credit Program, Dept. of Food and Agriculture, 1220 N Street Room 409, Sacramento, CA 95814.

Code 217, Solar Energy System. You may claim as much as 15% of the cost of a Solar Energy System, as figured on form FTB 3508 (*built into the software for the Premium Level*).

Repealed credits with carryover provisions. (*Road Map lines, supported by Form 3540.*) These credits have all expired, but carryover of unused credit from prior years is still available. *If you complete a Form 3540, the carryover you enter there will be posted here automatically.* Otherwise you can enter

the amounts here directly. The amounts not used this year are carried over to next year.

- Code 175, Agricultural products.** Originally figured on FTB 3534.
- Code 194, Employee ridesharing.** Originally figured on Form 3572.
- Code 182, Energy conservation.** Originally figured on FTB 3514.
- Code 191, Employer ridesharing: Large employer program.** Originally figured on FTB 3518.
- Code 192, Employer ridesharing: Small employer program.** Originally figured on FTB 3518.
- Code 193, Employer ridesharing: Transit pass credit.** Originally figured on FTB 3518.
- Code 160, Low-emission vehicles.** Originally as much as 55% of the cost of converting to low-emission vehicles, but you had to obtain certification from the California Energy Commission.
- Code 184, Political contributions.** Originally figured on Schedule P.
- Code 174, Recycling equipment.** Originally figured on FTB 3514, you could formerly claim as much as 40% of the cost of qualified equipment purchased before 1994.
- Code 186, Residential rental and farm sales.** Originally figured on FTB 3529.
- Code 171, Ridesharing.** The credit expired years ago.
- Code 200, Salmon & steelhead trout habitat restoration.** This credit expired just before the current tax year.
- Code 179, Solar pump.** The credit expired years ago, and is available only to farmers. It applies only to measures installed in 1981 through 1984.
- Code 178, Water conservation.** The credit expired years ago, and applies only to measures installed in 1980 through 1982.
- Code 161, Young infant.** Originally figured on Schedule P.

7 through 10, Section A2 Summary. Up to four credits used above are consolidated into lines 7 through 10. Each of the four lines consists of the following five columns:

- Code and Credit Name.** *(auto-calc)* Credit code numbers and credit names are generated here when any one or more of the above credits is claimed in section A2.
- Credit amount.** *(auto-calc)* The total credit is shown here and printed in column (a) of the official Schedule P.
- Credit used this year.** *(auto-calc)* Computed as the lesser of the credit amount for this line, column (a), and the tax balance for the last numbered line used on the schedule, column (c), and printed in column (b) of this line.
- Credit carryover.** *(auto-calc)* Computed as "credit amount" for this line, column (a), less "credit used this year" for this line, column (b). This is the amount that can be claimed next year, and is printed in column (d) of this line.

Overflow credits. If more than four credits have been claimed this year in section A2, the remaining total appears here. You must, in a supporting statement for this line, provide the same detail as above for these remaining credits.

11 Code 188, Credit for prior year minimum tax. You may claim this credit if you paid alternative minimum tax last year but have no alternative minimum tax this year.

Credit amount. Enter the result from FTB 3510 (*built into the software for the Premium Level*). This entry is printed in column (a) of Schedule P.

Credit used this year. (*auto-calc*) Computed as the lesser of the credit amount for this line, 11(a), and the tax balance for the last numbered line used on the schedule and printed in column (b) of line 11.

Credit carryover. (*auto-calc*) Computed as "credit amount" for line 11(a) less "credit used this year" for line 11(b). This is the amount that can be claimed next year, and is printed as line 11(d).

SECTION B - CREDITS THAT MAY REDUCE TAX BELOW TENTATIVE MINIMUM TAX. The current-year claims for the credits in this section are allowed to exceed line 8, but they cannot reduce tax any more than the amount of alternative minimum tax.

12 Line 1, or line 2 plus last tax balance. (*auto-calc*) If line 3 is zero, line 1 is used here. Otherwise, line 2 plus the tax balance on line 11 (column c) is used.

Line 12 is the tax balance that may be offset by credits in Section B.

B1 Credits that reduce net tax and have no carryover provisions. Credits in this section were formerly carryovers from Section A1. However, because of the change in California law, they now appear *only* here. Unused credits in this section are lost forever.

Qualify for Joint Custody Credit? You qualify for the credit if you could have filed under the filing status Joint Custody Head of Household had California not eliminated this category. This means that you must furnish more than half of the household expenses for a qualifying child, stepchild, or grandchild for at least 146 days, but no more than 219 days. You must also file single (or, if married filing separately, must have lived apart from spouse the entire year, as answered on Form 540). Note that the child need not be your dependent unless the child is married. See FTB Form 540 instructions for lines 28 through 30 for details.

13 Code 170, Credit for joint custody head of household. (*auto-calc*) If you answered Yes to the above qualifying question, and otherwise qualify based on filing status, this line is computed as 30% of an adjusted tax, but no more than \$327; otherwise, zero. The adjusted tax is the tax on line 24 of Form 540 less the amount of FTB 5870A tax included in line 23 of Form 540.

Credit used this year. *(auto-calc)* Computed as the lesser of the full credit amount and the tax balance for the last numbered line used on the schedule, and printed in column (b) of line 13.

Qualify for Dependent Parent Credit? You may be eligible for this credit if you were married at the end of the tax year, your spouse was not a member of your household during the last six months of the year, you file a separate return (filing status 3), and you furnished over half of the household expenses for your dependent parent's home. If you qualify, answer Yes to this question.

14 Code 173, Credit for dependent parent. *(auto-calc)* If you answered Yes to the above qualifying question, and otherwise qualify based on filing status, this line is computed as 30% of an adjusted tax, but no more than \$327; otherwise, zero. The adjusted tax is the tax on line 24 of Form 540 less the amount of FTB 5870A tax included in line 23 of Form 540.

Credit used this year. *(auto-calc)* Computed as the lesser of the full credit amount and the tax balance for the last numbered line used on the schedule, and printed in column (b) of line 14.

Meet age requirements for Senior Head of Household Credit. *(auto-calc)* Automatically Yes only if a senior exemption is claimed at line 9 of Form 540.

Meet death and filing requirements for Senior Head of Household Credit? You should answer Yes ONLY if you qualified as head of household in 2002 or 2003, and the person who qualified you for this filing status died during 2002 or 2003.

15 Code 163, Credit for senior head of household. *(auto-calc)* Computed based on the above two answers using the worksheet in the Form 540 instructions. The credit is the lesser of \$1,000 and 2% of taxable income on line 19 of Form 540. However, *NO* credit is allowed when AGI on line 17 of Form 540 exceeds \$53,084.

Credit used this year. *(auto-calc)* Computed as the lesser of the full credit amount and the tax balance for the last numbered line used on the schedule, and printed in column (b) of line 15.

16 Nonrefundable renter's credit. You may claim a credit for as much as \$120, as explain in our details for line 31 of Form 540. *You claim the credit by entering the number of qualifying persons above line 31 of Form 540, and the software does the rest.*

Credit used this year. *(auto-calc)* Computed as the lesser of the full credit amount and the tax balance for the last numbered line used on the schedule, and printed in column (b) of line 16. This result is posted to line 31 of Form 540.

17 Code 212, Teacher retention credit. *(SUSPENDED for 2004 and 2005.)* This credit was suspended for tax year 2002, reinstated for 2003, but suspended once again for tax years 2004 and 2005. As a result, no data entry lines are available this year.

B2 Credits that reduce net tax and have carryover provisions. All of these credits are carried over to the next year except for the last two, which are applied to Section C.

Current Credits. The following credits are credits for 2004 expenses:

Code 197, Child adoption. (*Supported by the Child Adoption Credit Worksheet, Figure CA-3.*) In the year of adoption, half of the cost of adopting a child is reimbursed as a credit, up to a maximum of \$2,500 for each qualified adoption. Supporting worksheets compute the credit allowable credit for you. Because the limitation is applied separately for each child, you must use a separate worksheet for each separate adopted child. The worksheet helps determine your eligibility for the credit through selected questions, and provides data entry lines for the only expenses that are qualified: fees to a qualified agency, unreimbursed medical expenses for the child, and travel expenses for the adoptive family. See FTB Form 540 instructions for lines 28 through 31 for other details.

Code 176, Enterprise zone hiring & sales and use tax. You must file FTB 3805Z (not built into the software) with the return, and enter the result on the enterprise zone part of that form here. (While the Program Area Hiring & Sales or Use Tax Credit, Code 177, no longer appears in the instructions for Schedule P, it was actually rolled over into the Enterprise Zone Employee Credit, Code 176.)

Code 172, Low-income housing. You must file FTB 3521 (*built into the software for the Premium Level*) with the return, and enter the result of that form here.

Code 210 Targeted Tax Area (TTA) Hiring & Sales or Use Tax. This business incentive for targeted areas is claimed through FTB Form 3809 (not built into the software).

Code 213, Natural heritage preservation. You must file FTB 3503 (not built into the software) with the return, and enter the result of that form here.

Code 183, Research. You must file FTB 3523 (*built into the software for the Premium Level*) with the return, and enter the result of that form here.

Repealed credits carried over to 2004. (*Road Map lines, supported by Form 3540.*) These credits have all expired, but carryover of unused credit from prior years is still available. *If you complete a Form 3540, the carryover you enter there will be posted here*

| CHILD ADOPTION CREDIT | |
|--------------------------------|-----|
| Child's name | |
| Citizen or legal res of US? No | |
| In custody of qlfd. agency? No | |
| Cred carryover fr prior yr | 0 |
| If adoption order THIS yr: | |
| Fees of the qlfd. agency.. | 0 |
| Unreimbursed medical expns | 0 |
| Adoptive family travel exp | 0 |
| Total allowable credit: | |
| 1 Total qualified expenses.. | 0 |
| 2 Credit percentage - 50%... | .50 |
| Credit before limitation.. | 0 |
| 3 Credit amount..... | 0 |
| Carryover to next year.... | 0 |

Figure CA-3. Child Adoption Credit Worksheet

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Schedule P

automatically. Otherwise you can enter the amounts here directly.

Code 199, Manufacturers' investment. Originally figured on FTB 3535.

Code 196, Commercial solar electric system. Originally figured on FTB 3556.

Code 159, Los Angeles Revitalization Zone (LARZ) hiring & sales and use tax. Originally figured on FTB 3806.

Code 185, Orphan drug. Originally figured on FTB 3528.

Repealed credits carried over first to Section B2, then to Section C. (*Road Map lines, supported by Form 3540.*) These credits have all expired, but carryover of unused credit from prior years is still available. *Any amounts not used in section B2 can be carried over to Section C, which is less limited than Section B2. If you complete a Form 3540, the carryover you enter there will be posted here automatically.* Otherwise you can enter the amounts here directly.

Code 180, Solar energy. Originally figured on FTB 3805L, but expired on January 1, 1987.

Code 181, Commercial solar energy. Originally figured on FTB 3805L.

18 through 21, Section B2 Summary. Up to four credits used above are consolidated into lines 18 through 21. Each of the four lines consists of the following five columns:

Code and Credit Name. (*auto-calc*) Credit code numbers and credit names are generated here when any one or more of the above credits is claimed in section B2.

Credit amount. (*auto-calc*) The total credit is shown here and printed in column (a) of the official Schedule P.

Credit used this year. (*auto-calc*) Computed as the lesser of the credit amount for this line, (a), and the tax balance for the last numbered line used on the schedule, (c), and printed in column (b) of this line.

Tax balance. (*auto-calc*) Computed as "tax balance" for the last numbered line used on the schedule, column (c), less "credit used this year" for this line, column (b), and printed in column (c) of this line.

Credit carryover. (*auto-calc*) Computed as "credit amount" (a) for this line, less "credit used this year" (b). This is the amount that can be claimed next year, and is printed in column d of this line.

Overflow credits. If more than four credits have been claimed this year in section B2, the remaining total appears here. You must, in a supporting statement for this line, provide the same detail as above for these remaining credits.

B3 Credits that reduce net tax and have no carryover provisions. For the sole line in this part of Section B, the unused credit cannot be carried over to the next year:

22 Code 187, Other state tax credit. (*Road Map line, supported by Schedule S.*) Five copies of Schedule S are built into the software, for reporting income tax paid to up to five states. The result on line 12 of all Schedules S combined is posted to column (a) of this line.

Credit used this year. *(auto-calc)* Computed as the lesser of the full credit amount (line 22(a)) and the tax balance for the last numbered line used on the schedule, and printed in column (b) of line 22.

SECTION C - CREDITS THAT MAY REDUCE ALTERNATIVE MINIMUM TAX.

Claims for solar energy credits are allowed to reduce the alternative minimum tax. They are carried over from Section B2 to lines 24 and 25, below.

23 AMT from Schedule P Part II, line 26. *(auto-calc)* The result on Schedule P page 1 before reduction by these credits is posted here.

24 Code 180, Solar energy credit carryover from Section B2. *(auto-calc)*
The carryover is posted here automatically.

Credit used this year. *(auto-calc)* Computed as the lesser of the above total credit for line 24 and the amount on line 23.

Credit carryover. *(auto-calc)* Computed as the total credit on line 24 less the above "credit used this year." This is the amount that is carried over to next year.

25 Code 181, Commercial solar energy credit carryover from Section B2. *(auto-calc)* The carryover is posted here automatically.

Credit used this year. *(auto-calc)* Computed as the lesser of the above total credit for line 25 and the tax balance at line 24.

Credit carryover. *(auto-calc)* Computed as the total credit on line 25 less the above "credit used this year." This is the amount that is carried over to next year.

26 Adjusted AMT. *(auto-calc)* Computed as the tax balance at line 25. The result at line 26 is posted to Schedule P page 1 and used in place of line 26 of Schedule P page 1 for posting to line 35 of Form 540.

ALLOCATION TO FORM 540. *(auto-calc lines)* The current-year totals are reflected in lines 28 through 31 of Form 540. The name and amount for the first two credits are posted to lines 28 and 29, and the total of any remaining credits, except for the renter's credit, is posted to line 30. The renter's credit at line 16 of Schedule P, Part III, is posted to line 31 of Form 540.

Schedule S / Other State Tax Credit

Purpose is to avoid double taxation. This schedule is used to report income taxes paid to another state on income that is taxed by California as well. The portion of tax paid to the other state on income taxed by both states is used to offset the portion of tax computed on the California return for the same income. NOTE: You must attach to your California return a copy of the tax return filed with the other state. Five copies of Schedule S are built into the software so that you can report double-taxed income for as many as five states.

PART I - DOUBLE TAXED INCOME. Details on double taxed income are reported here.

- 1 Total double taxed by California.** *(Supported by the Double Taxed Income Worksheet, Figure CA-4.)* You must complete a separate supporting worksheet for each double taxed income item.
- 1 Total double taxed by other state.** *(Supported by the Double Taxed Income Worksheet, Figure CA-4.)* The same set of worksheets supports this line as well.

| DOUBLE TAXED INCOME WRKSHT | |
|-----------------------------|---|
| a. Income item des | |
| b. Taxable by California | 0 |
| c. Taxable other state..... | 0 |

Double Taxed Income Worksheet. *(Figure CA-4)* This worksheet is just a simple itemized list, but with two amount columns:

Figure CA-4. Double Taxed Income Worksheet

a Income item description. Enter a description (up to 25 characters) for each double taxed income item on a separate worksheet page.

b California amount. Enter California amount for the item.

c Other state amount. Enter the other state amount for the item.

The total of line b from all worksheets is used in line 3, below, and the total of line c from all worksheets is used in line 8.

PART II - OTHER STATE TAX CREDIT. The computation of credit to be posted to Schedule P is computed here:

- 2 California tax liability.** *(auto-calc)* Computed as the tax balance on line 24 of Form 540, less total credits on line 33 of Form 540 (but with any Other State Tax Credit included in line 33 removed).
- 3 Double taxed income taxable by California.** *(auto-calc)* Taken from the total for California at line 1, above.
- AGI on Form 540, line 17.** *(auto-calc)* As indicated.
- Lump sum distributions on Schedule G-1.** If you used Schedule G-1 to compute tax you must report the income taxed here, since it is not included in AGI.
- 4 California adjusted gross income.** *(auto-calc)* Computed as the sum of the above two lines.
- 5 Divide line 3 by line 4 (100 % maximum).** *(auto-calc)* Computed as indicated, expressed as a percentage limited to no more than 100%.

- 6 Multiply line 2 by % on line 5.** *(auto-calc)* As indicated.
- 7 Income tax paid to.** Enter here the name of the other state here.
- 7 Amount paid to above state.** Enter here the dollar amount of tax paid to the other state for the same tax year the income is taxed by California.
- 8 Double taxed income taxable by other state.** *(auto-calc)* Taken from the total for other state at line 1, above.
- 9 Adjusted gross income taxable by other state.** Enter the AGI for the income tax return you file with the other state.
- 10 Divide line 8 by line 9 (100 % maximum).** *(auto-calc)* Computed as indicated, expressed as a percentage limited to no more than 100%.
- 11 Multiply line 7 by % on line 10.** *(auto-calc)* Computed as indicated.
- 12 Other state tax credit.** *(auto-calc)* Computed as the lesser of line 6 or line 11, and posted to line 22 of Schedule P, Part III.

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Forms 3501, 3504, and 3505

***Form 3501 / Employer Child Care Program/Contribution Credit**

Purpose. This form is used by employers to claim a credit for their contributions to child care activities, including employee child care programs and contributions to child care services. The credit is generally 30% of the qualifying costs, up to a maximum of \$50,000. The form is also used to figure recapture for credit previously claimed on a child care facility that ceased operation within 5 years of its establishment.

*** Included in Premium Level software ONLY.** This form is only built into the Premium Level version of the California Supplement. It is detailed in the separate *Premium Level Supplement 2005*. (When available, Form 3501 is accessible through the Road Map from Schedule P, page 2, at the line for credit 189 in Section A2 of Part III.)

***Form 3504 / Long-Term Care Credit**

Purpose. This form is used by taxpayers to claim up to \$500 of credit for providing care to individuals who require long-term care.

*** Included in Premium Level software ONLY.** This form is only built into the Premium Level version of the California Supplement. It is detailed in the separate *Premium Level Supplement 2005*. (When available, Form 3504 is accessible through the Road Map from line 4 of Schedule P, page 2 – the line for credit 214 in Section A1 of Part III.)

Form 3505 / Teachers Retention Credit

SUSPENDED FOR 2004 AND 2005. This credit was suspended for tax year 2002, reinstated for tax year 2003, and is once again suspended for tax years 2004 and 2005. When not suspended, it provides a credit against income tax for credentialed teachers of grades kindergarten through 12th grade. The credit can amount to as much as \$1,500 for each spouse who is a qualifying teacher. The credit is reduced if years of service is less than 20 years or the portion of your income tax attributable to teaching is less than \$3,000.

Wages from teaching and years of service control the calculations. The credit is nominally 50% of the *pro rata* portion of tax liability that is associating with the teaching job. You must therefore determine the total wages from teaching alone that you receive. The credit is then limited by a ceiling that depends on years of service, with the ceiling as high as \$1,500 for teachers with 20 or more years of service. *When not suspended, this form is accessible through the Road Map from page 2 of Schedule P (at line 17 of Part III).*

Form 3506 / Child & Dependent Care Expenses Credit

Child care credit has its own form. California provides its own form for the child care credit. Since the credit is generally just a percentage of the federal credit (federal Form 2441), the computation of the credit on this form duplicates the computation on the federal form until the percentage is applied. The percentage ranges from 50% for California AGI of \$40,000 or less to zero for California AGI above \$100,000. The credit is posted to Form 540 lines 42 through 45.

CAUTION: Additional reporting requirements. There are a number of required entries that do not appear on the federal Form 2441, so you must supply additional details:

- (1) California requires that the SSNs of the first two qualifying children appear on Form 540. While the SSNs exist on the worksheets for line 2 of federal Form 2441, and are therefore translated to the California worksheets, the SSNs do NOT appear on Form 2441 itself, and therefore cannot be translated to the California Form 3506 itself. Therefore, after translation from the federal return you must access and view each Qualifying Person Worksheet for line 2 of Form 3506 so that the SSNs can be posted to Form 3506 itself.
- (2) You must provide the telephone number of each care provider and identify whether the care provider is a person or an organization.
- (3) You must provide the year of birth of each child, or, if disabled, identify the child as disabled.
- (4) You must enter the percentage of time spent in your California home.

CAUTION: Some taxpayers do not qualify. While the software automatically translates this form from the Form 2441 in the federal return and gives most taxpayers a credit if their Form 2441 showed a credit, there is one important condition you must meet to qualify for the credit. The care must have been provided in California. If not, you must zero out the translated form, then remove it from the return with out File Manager. (The requirement for the care to take place in California has replaced the former residency requirement. You no longer have to maintain a home in California in order to take the credit. However, you must have earned wages or self-employment income in California.)

***Form 3508 / Solar or Wind Energy System Credit**

Purpose. This form is used to claim credit for up to 7.5% of the cost of purchase and installation of a solar or wind energy system.

*** Included in Premium Level software ONLY.** This form is only built into the Premium Level version of the California Supplement. It is detailed in the separate *Premium Level Supplement 2005*. (When available, Form 3508 is accessible through the Road Map from Schedule P, page 2, at the line for credit 217 in Section A2 of Part III.)

***Form 3510 / Credit for Prior Year Alternative Minimum Tax**

Purpose. This form, which is analogous to Federal Form 8801, provides a credit for prior-year AMT when the current-year tentative minimum tax is less than the regular tax.

*** Included in Premium Level software ONLY.** This form is only built into the Premium Level version of the California Supplement. It is detailed in the separate *Premium Level Supplement 2005*. (When available, Form 3510 is accessible through the Road Map from line 11 of Schedule P, page 2 -- the line for credit 188 in Section A2 of Part III.)

Form 3519 / Automatic Extension

An extension of time to file is automatic, without this form. Unlike the IRS, California's FTB no longer requires you to apply for an extension of time to file. Instead, a 6-month extension of time to file is automatic as long as you file by October 17, 2005. However, an extension of time to file does not give you extension of time to pay! You still must pay any remaining tax due by April 15, 2005, enclosing the Form 3519 voucher with your payment, in order to avoid penalties and interest.

California Form 3519 is similar to federal Form 4868 in the software. Even though the filing requirements are different for the California form, the operation of the software is quite similar to that for Form 4868. It is used to estimate the tax liability when the return is not yet complete and could be far from the final version. As a result, we do not complete this form automatically but give you helpful guidance instead. It is up to you to make the final determination of estimates to use in determining how much you need to pay to the FTB. (See the section on Form 4868 in Chapter 2 of the regular Tax Forms Guide 2005 Edition for details of the analogous federal form.)

Data entry differences from the federal form are few. Because California requires this form only if more tax is due, this form has its sections in a different order than the federal form.

Tax payment worksheet. The first section is the estimate of tax liability. Like the federal form, the amounts that exist on the return in its current state appear above the data entry lines for Form 3519 as guidance. But since these amounts could be far from what you expect the final return to reflect, you are free to enter any amounts on the data entry lines below them.

When to file Form 3519. You must normally file this form with the tax due by April 15, 2005. However, if you are living or traveling outside the U.S. on that date, you have until June 15th to file and pay all tax due. Unlike the federal Form 4868, it is *NOT* necessary to work outside the U.S. or be in military service outside the U.S. Travel alone is a sufficient excuse for delayed filing. However, if you do not pay all tax due by June 15, you will be subject to the usual penalties and interest.

***Form 3521 / Low-Income Housing Credit**

Purpose. This form, which is analogous to Federal Form 8586, provides a credit for placing in service a building with a qualified amount of low-income housing.

*** Included in Premium Level software ONLY.** This form is only built into the Premium Level version of the California Supplement. It is detailed in the separate *Premium Level Supplement 2005*. (When available, Form 3521 is accessible through the Road Map from Schedule P, page 2, at the line for credit 172 in Section B2 of Part III.)

***Form 3523 / Research Credit**

Purpose. This form, which is analogous to Federal Form 6765, provides a credit for increasing the technological research performed by your company.

*** Included in Premium Level software ONLY.** This form is only built into the Premium Level version of the California Supplement. It is detailed in the separate *Premium Level Supplement 2005*. (When available, Form 3523 is accessible through the Road Map from Schedule P, page 2, at the line for credit 183 in Section B2 of Part III.)

***Form 3526 / Investment Interest Expense Deduction**

Purpose. This form, which is analogous to Federal Form 4952, is used to figure the amount of interest applicable to maintaining investments that can be deducted in the current year and to figure the amount of carryover to the next year.

*** Included in Premium Level software ONLY.** This form is only built into the Premium Level version of the California Supplement. It is detailed in the separate *Premium Level Supplement 2005*. (When available, Form 3526 is accessible through the Road Map from our Worksheet A at the line "Investment adjustment on California Form 3526," and is reflected in the adjustment at line 40 of Schedule CA.)

***Form 3533 / Change of Address**

Purpose. This form, which is analogous to Federal Form 8822, is used to report to the FTB any change of address for your business or personal tax returns.

*** Included in Premium Level software ONLY.** This form is only built into the Premium Level version of the California Supplement. It is detailed in the separate *Premium Level Supplement 2005*. (When available, Form 3533 is accessible only through the Forms Menu because it is a stand-alone form not normally filed with the Form 540 return)

***Form 3535 / Manufacturer's Investment Credit**

Purpose. The manufacturer's investment credit expired at the end of 2003, so the current Form 3535 is used only to report a carryover of the credit from prior years.

*** Included in Premium Level software ONLY.** This form is only built into the Premium Level version of the California Supplement. It is detailed in the separate *Premium Level Supplement 2005*. (When available, Form 3535 is accessible through the Road Map through the last line of Form 3540 – the line for credit 199. The credit then flows through to Schedule P, page 2, at the line for credit 199 in Section B2 of Part III.)

Form 3540 / Credit Carryover Summary

Consolidates carryovers from expired credits. This form replaces a number of forms for expired credits. Forms for expired credits typically live long after their credits due to carryover provisions for unused credits. However, instead of retaining the old forms, the FTB uses this one form for reporting credit carryovers from a number of unrelated credits. Unless you file Schedule P, this form is required if you claim any of the carryover credits listed on this form. If you file Form 3540 and there is no Schedule P for the return, the credits used this year on this form are automatically posted to Form 540 lines 28 through 30. CAUTION: Lines on Schedule P Part V that are supported by this form through the Road Map will get their entries from this form when this form exits, and override any entries you make directly on Schedule P.

Schedule P may automatically replace Form 3540. If you have more than two credits or are subject to the alternative minimum tax, you are required to complete Schedule P, where the credits on these and other forms are consolidated before posting to Form 540. In fact, the software automatically generates Schedule P when it appears to be necessary. If a Schedule P exists, the credits entered on Form 3540 are consolidated with any other credits entered on Schedule P, and the calculations for amounts claimed this year, tax balances, and carryovers are performed on Schedule P instead of Form 3540. In addition, Form 3540 is intentionally omitted from the official print-out in this case, as required by the FTB, and all required information is shown on Schedule P instead. When a Schedule P, page 2, exists for the return, the question on Form 3540 labeled "See Schedule P for claims/carryovers" will be automatically answered Yes and no calculations will appear on Form 3540.

All carryovers follow the same format. Twenty one separate credit carryovers are shown on this form, each following the same format 3-column format. Our format follows the FTB's 3-column format with an added line showing the ongoing tax balance in each part. Each credit has the following four lines:

a Carryover from prior years. Enter here the carryover from the prior tax return for this credit. This carryover can be found on the prior-year form for the credit or Part V of last year's Schedule P. If a Schedule P, Part V, exists *this* year for the return, this entry is posted there and the below lines are left blank.

b Amount claimed on current year tax return. (auto-calc) Normally computed as the lesser of the above carryover and the tax balance remaining after the preceding credit in the FTB order is claimed. However, if Schedule P page 2 exists for this return, no calculation appears here.

Tax balance. (auto-calc) Normally computed as the prior tax balance less the above credit, but zero if Schedule P page 2 exists for this return.

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Forms 3540, 3548, and 3553

c Carryover to future years. (*auto-calc*) Normally computed as the carryover entered in line a less the credit used this year (line b), but zero if Schedule P page 2 exists for this return.

Note that two of the carryovers apply only to corporations -- credit carryovers for Technological Property Contribution, code 201, and Contribution of Computer Software, code 202 -- and so they are blocked from data entry and calculation in the software.

Summary. The names and amounts for the claimed credits are shown on the last screen of Form 3540 just like they are on Schedule P. Moreover, if Schedule P page 2 exists, the amounts shown in that summary override the ones that would be computed from Form 3540 alone. The resulting entries are posted to Form 540 lines 28 and 29. If more than two credits are claimed on Form 3540, Schedule P page 2 is automatically generated and completed upon the final recalculation of the return.

***Form 3548 / Disabled Access Credit for Eligible Small Businesses**

Purpose. This form, which works in concert with federal Form 8826, provides a credit for expenditures to provide access to disabled individuals. The credit is 50% of the qualified expenses up to \$250. By contrast, the federal credit is 50% of the qualified expenses that exceed \$250 (up to a \$10,250 maximum).

*** Included in Premium Level software ONLY.** This form is only built into the Premium Level version of the California Supplement. It is detailed in the separate Premium Level Supplement 2005. (When available, Form 3548 is accessible through the Road Map through Schedule P, page 2, at the line for credit 205 in Section A2 of Part III.)

***Form 3553 / Enterprise Zone Employee Credit**

Purpose. This form provides a credit to employees who work within a California enterprise zone. The credit is generally 5% of up to \$10,500 of qualified wages, but is reduced by a portion of wages earned outside the enterprise zone.

*** Included in Premium Level software ONLY.** This form is only built into the Premium Level version of the California Supplement. It is detailed in the separate Premium Level Supplement 2005. (When available, Form 3553 is accessible through the Road Map through line 6 of Schedule P, page 2 -- the line for credit 169 in Section A1 of Part III.)

Form 3800 / Tax for Children with Investment Income

Children must be taxed at parent's tax rate on some income. Like federal Form 8615, this form is used to compute tax for children under 14 years of age who have unearned income of more than \$1,600.

Form 3800 matches federal Form 8615, but adjustments necessary. Even though the California form matches the federal equivalent even to the extent of using the same line numbers, the incomes translated from the federal Form 8615 may require readjustment if the parent or other children had any adjustments on their California Schedule CA. The most likely adjustments are highlighted here, but you should refer to the details for Form 8615 in Chapter 2 of the Tax Forms Guide 2005 Edition for other details.

Parent's taxable income. Translated from line 6 of federal Form 8615, this entry will have to be readjusted if the parent's California taxable income is different from the parent's federal taxable income. This entry should match line 19 on the parent's Form 540.

1 Child's investment income. *(auto-calc)* Computed from:

Child's AGI on Form 540, line 17. *(auto-calc)* Taken from Form 540 as indicated.

Child's California earned income. *(auto-calc)* Posted from "Total Calif. earned income" on screen 4 of Form 540.

Other adjustments. If the total AGI less the computed total earned income, above, does not reflect the entire investment income for the child, enter any additional adjustment here.

Line 1 is then the AGI less the earned income plus the above adjustment.

2 If DID NOT itemize, \$1,600. *(auto-calc)* Computed from:

Itemized deductions on Form 540. *(auto-calc)* This is the amount posted to Form 540 from line 43 of Schedule CA.

Itemized deduction, if used. *(auto-calc)* Identical to the preceding amount if the itemized deduction is used at line 18 of Form 540 rather than the standard deduction. Otherwise, zero.

Investment part of itemized deductions. Translated from the corresponding entry on federal Form 8615, this entry will have to be modified if any of the adjustments on line 41 of Schedule CA relate to the investment part of itemized deductions.

If you itemize deductions, line 2 is computed based on a formula that involves the last of the above three entries. Otherwise the result is \$1,600.

7 Form 3800, line 5 for all other children. Translated from line 7 of federal Form 8615, this entry will have to be readjusted if the California taxable income for any of the children is different from their federal taxable income.

Tax computations automatic. The rest of the form is automatic. The result of this form is posted to Form 540 and used as the tax on line 20, in place of the tax table amount, if the taxpayer is liable for the Form 3800 tax.

Form 3801 / Passive Activity Loss Limitations

Conformity, but not simplicity. Because California had conformed to the federal passive activity loss limitations until 2002, Form 3801 formerly paralleled federal Form 8582 even to the point of line numbers on page 1. However, California has NOT conformed to the federal provision for Commercial Revitalization Deductions from Rental Real Estate Activities. Furthermore, because California amounts can differ from federal amounts *before* application of the passive activity rules, the FTB has designed its own set of worksheets to complete. As a result, the form is even more complex than the federal form. In fact, California adjustments are often necessary for businesses and investors because of the past differences in the depreciation laws.

Page 1 is fully automatic for most returns. When a federal Form 8582 exists with the return, Form 3801 is translated from that form. However, because of adjustments for law differences, it is possible for Form 3801 to be required even when the federal Form 8582 is not. If you made any entries directly on Form 8582 for "Other passive activities," you may have to adjust those translated entries. However, entries from federal Schedules C, D, E, F, and Forms 4797 and 4835 are automatically readjusted when the California return is completed. Like the federal equivalent, this form may not be complete and accurate until the final recalculation of the return, because it involves amounts from several other forms and worksheets. For further details, refer to the details for Form 8582 in Chapter 17 of the main manual.

Entry at line 6 required if no federal Form 8582 exists. In the unusual case where a California Form 3801 is required while a federal Form 8582 is not, you will have to make an entry above line 6 for "Federal modified AGI." See the details for Form 8582 in Chapter 2 of the Tax Forms Guide 2005 Edition for more information on how to determine this entry. Note that California uses the federal amount directly, rather than an adjusted version based on California amounts.

Page 2 is unique to California. In addition to page 1 of Form 3801, which is similar to page 1 of federal Form 8582, California now requires you to file a second page that shows how differences between federal and California amounts affect individual activities, forms, and schedules. Because *Tax Preparer* is already fully automated, the second page is not required for any calculations in the return. It is therefore included in the software only to comply with the FTB instructions to include it with the return.

Passive Activity Worksheets. (*Figure CA-5*) The first part of page 2 of Form 3801 is a table that shows California adjustments to activities before application of the passive activity rules. We provide a set of Passive Activity Worksheets in the same format as this table, allowing you to provide the data the FTB requests if you so desire. Nevertheless, the calculations and validity of the return are unaffected if you fail to complete these worksheets. All amounts for these worksheets are visible on screens 2 through 6 of California Form 3801 and federal Form 8582. We recommend that you generate our

quick-print printouts, which show all information on the screens, for each of these forms, and complete the worksheets as follows: (A quick-print printout is generated by pressing the Quick-Print Key, F6 or ctrl-P, while viewing a screen of the form you want to print.)

| PASSIVE ACTIVITY WORKSHEET | | |
|----------------------------|------------------------|---|
| a. | Passive Activity | |
| b. | Federal Schedule..... | |
| c. | Calif. Schedule..... | |
| d. | Federal Amount..... | 0 |
| e. | Calif. Adjustment..... | 0 |
| f. | Calif. Amount..... | 0 |

a. Passive Activity.

Enter an appropriate description based on the title on the screen for the section you are reporting here. Use Table CA-3 as a guideline. You

Figure CA-5. Passive Activity Worksheet

can group like items together. For example, if you report rental real estate in Part I of federal Schedule E and you sold the property, you can combine the operating income on Schedule E with the sale income on Form 4797 (California Schedule D-1), using a single Passive Activity Worksheet for the entire activity.

- b. Federal Schedule.** Most items on federal Form 8582 relate to a particular form or schedule and are identified in the titles on the screen. If you combined amounts from different forms for the same activity onto one worksheet, list all such forms, such as E & 4797 for the preceding example.
- c. Calif. Schedule.** Most items on California Form 3801 have no official California form to which they relate. You can leave the entry blank for those cases. But you should enter D, D-1, and 3805P when they apply.
- d. Federal Amount.** For activities whose amounts are shown on screens 2 and 3 of Form 8582, enter the total of "Gain for line 1a" minus "Loss for line 1b" minus "Prior unallowed for 1c." For all other activities enter the analogous total for lines 2a, 2b, and 2c.
- e. California Adjustment.** For activities whose amounts are shown on screens 2 and 3 of FTB 3801, enter the total of "Gain for line 1a" minus "Loss for line 1b" minus "Prior unallowed for 1c" minus the preceding entry for line d. For all other activities enter the analogous total for lines 2a, 2b, and 2c less line d, above.
- f. California Amount.** (*auto-calc*) Computed as line d less line e.

Table CA-3. Entries for column (a) of Passive Activity Worksheets

| | | |
|----------------|-----------------|--|
| FTB3801 screen | Transfers from | Suggested entry for line a of Passive Activity worksheet |
| 2 | Sch. E Part I | Rental real estate |
| 2 | Sch. E Part II | Partnership rental real |
| 2 | Sch. E Part III | Estate/trust rental real |
| 3 | Schedule D-1 | Rental real estate (or describe property sold) |
| 3 | fed Form 4835 | Farm rental income |
| 3 | Form 3805E | Rental real estate (or describe property sold in installments) |
| 4 | Schedule C | Business |
| 4 | Schedule D | (describe property sold) |
| 5 | Sch. E Part I | Rental real estate |
| 5 | Sch. E Part II | Partnership rental real |
| 5 | Sch. E Part III | Estate/trust rental real |
| 5 | Schedule F | Farm |
| 6 | Schedule D-1 | (describe property sold) |
| 6 | fed Form 4835 | Farm rental income |
| 6 | Form 3805E | (describe property sold under installment sale) |

California Adjustment Worksheets. The remainder of the page 2 of Form 3801 summarizes passive and nonpassive adjustments *after* application of the passive loss rules for activities that are reported on Schedules C, E, and F. This reporting is desired by the FTB because California has no equivalent to these schedules, so their adjustments appear only as grand totals on Schedule CA. *Tax Preparer* has worksheets in this California Supplement to show the details of the adjustments. All amounts for the California Adjustment Worksheet are therefore available from a viewing of Worksheets C, E, and F. The California Adjustment Worksheets are therefore fully automated and require no manual entry. (Note that these worksheets are *not* automated for Apple II versions of the software because of system limitations. All lines are therefore manual entry lines for the Apple software.)

*Form 3801-CR / Passive Activity Credit Limitations

Purpose. This form, which is analogous to Federal Form 8582-CR, imposes limitations on credits for passive activities.

* **Included in Premium Level software ONLY.** This form is only built into the Premium Level version of the California Supplement. It is detailed in the separate Premium Level Supplement 2005. (When available, Form 3801-CR is accessible only from the Forms Menu, not through the Road Map.)

Form 3803 / Parent's Election to Report Child's Interest and Dividends

Full conformity to federal Form 8814. California Form 3803 now conforms fully to the federal equivalent, except for the tax rate. California taxes the first \$800 of the child's interest and dividend income at 1%, in contrast with the federal 15% rate. You can therefore consult the details for federal Form 8814 in Chapter 2 of the Tax Forms Guide 2005 Edition. *Form 3803 is accessible through the Road Map at line 20 of Form 540.*

Form 3805E / Installment Sale Income

Near conformity to federal Form 6252. California Form 3805E *appears* to conform fully with the federal equivalent, even to the extent of line numbers and descriptions. However, looks are deceiving because California has not yet conformed to recent changes in the federal law. California has conformed to few of the changes to the Internal Revenue Code by the Restructuring and Reform Act of 1998, none of the Tax and Trade Relief Extension Act of 1998, none of the Miscellaneous Trade and Technical Corrections Act of 1999, and none of the Ticket to Work and Work incentives Improvement Act of 1999. In particular, California does not conform to the federal modification of the pledge rules per the Ticket to Work and Work Incentives Act of 1999. (California did not conform to the federal disallowance of the installment method for accrual basis taxpayers, but the federal government has since retroactively repealed that disallowance.) Note also that interest on deferred tax (Section 453, 453A) should be included on Form 540, line 34 as an additional tax. *Form 3803E is accessible through the Road Map at line 1a of Schedule D and lines 4, 10, and 15 of Schedule D-1.*

Automatic for most taxpayers. In spite of the specific differences cited above, California law is in general conformance with federal law. As a result, the form is automatically translated from the federal form, and is automatically linked with Schedule D-1 in the same way as federal Form 6252 is automatically linked with Form 4797. As a result any adjustments on Schedule D-1 for differences between California and federal law are automatically reflected in Form 3805E. It should therefore not be necessary to make adjustments to Form 3805E for most sales in 1987 or later. Nevertheless, *if Part II is used for sales prior to 1987, you may have to make adjustments to reflect past differences in the law.* Since the form is so much like federal Form 6252, see the details for Form 6252 in Chapter 2 of the main Tax Forms Guide 2005 Edition for more information. (CAUTION: You must pay interest on deferred tax on certain installment obligations, but this interest is not figured on Form 3805E. See FTB instructions for details.)

Form 3805P / Additional Tax on Qualified Plans (IRAs, etc)

Only distributions are taxed, unlike federal Form 5329. This form is used to compute an additional tax on certain withdrawals (distributions) from IRAs and other retirement plans, annuities, modified endowment contracts, and medical savings accounts (MSAs). It is used to enforce the tax rules for such plans, assessing a penalty for not following the rules. However, whereas the federal Form 8615 assesses penalties for excess contributions and accumulations in addition to distributions, California Form 3805P assesses penalties only for distributions. Early distributions are reported in Part I, Ed IRA distributions not used for allowed education purposes are reported in Part II, and MSA distributions not used for allowed medical purposes are reported in Part III. See FTB instructions for Form 3805P for details. *Form 3803 is accessible through the Road Map at line 36 of Form 540.*

California Form 3805P Parts I and II match federal Form 5329 Parts I and II. Parts I and II of California Form 3805P reproduce Parts I and II of federal Form 5329 line for line, except for the tax rates applied at lines 4 and 8. The amounts subject to penalty are therefore taken automatically from the federal Form 5329 through our translation of that form. The tax rate applied for California at line 4 is 2-1/2% for most retirement plans, or 6% for SIMPLE plans, in contrast with the federal rates of 10% and 25%, respectively. The tax rate applied at line 8 is 2-1/2%, in contrast with the federal rate of 10%. See the details for Form 5329 in Chapter 2 of the Tax Forms Guide 2005 Edition for more information on Parts I and II of Form 3805P.

Part III, Tax on distributions from Archer Medical Savings Accounts (MSAs). This part is unique to the California form, but depends on federal Form 8853 (Medical Savings Accounts and Long-Term Care Insurance Contracts) for its entries.

9 Taxable MSA distribution from federal Form 8853, line 8. Enter amount from the federal form as indicated.

10a Do you meet any of the exceptions to the 10% tax? California conforms fully to the federal exceptions. Answer Yes here only if you checked the box on federal Form 8853, line 11a. See the IRS Instructions for federal Form 8853 for details.

10b If not, multiply line 9 by 10%. (*auto-calc*) Computed as one-tenth of line 9 if the above answer is No. Otherwise, computed as zero.

Summary of Parts I through III. The results from all three parts of Form 3805P are summed here.

Total tax for Form 540, line 36. (*auto-calc*) Computed as the sum of lines 4, 8, and 10b, this result is posted to Form 540 for inclusion in line 36 (along with other taxes).

Extra line for personal memos. Provided for supporting statements that will not be printed with the official return.

***Form 3805V / NOL Computation and NOL and Disaster Loss Limitations**

Purpose. This form, which is analogous to Federal Form 3621, is used to figure a deduction from income as a result of carryovers from years with a negative taxable income.

*** Included in Premium Level software ONLY.** This form is only built into the Premium Level version of the California Supplement. It is detailed in the separate *Premium Level Supplement 2005*. (When available, Form 3805V is accessible through the Road Map at lines 21b and 21d of Schedule CA.)

***Form 3805Z / Enterprise Zone Deduction and Credit Summary**

Purpose. This form is used to figure a deduction and a credit for business expenses in a California enterprise zone.

*** Included in Premium Level software ONLY.** This form is only built into the Premium Level version of the California Supplement. It is detailed in the separate *Premium Level Supplement 2005*. (When available, Form 3805Z is accessible through the Road Map at line 21e of Schedule CA.)

***Form 3806 / LARZ Deduction and Credit Summary**

Purpose. This form is used to figure a deduction and a credit for business expenses in a Los Angeles Revitalization Zone.

*** Included in Premium Level software ONLY.** This form is only built into the Premium Level version of the California Supplement. It is detailed in the separate *Premium Level Supplement 2005*. (When available, Form 3806 is accessible through the Road Map at line 21e of Schedule CA.)

Form 3885A / Depreciation and Amortization Adjustments

Conformity from 1987 through Jan. 1, 1993, and starting January 1, 1997, but not otherwise. California adopted the ACRS method for property placed in service in 1987 or later. This means that depreciation claimed on the federal return for newly acquired property will be the same on the California return for most property. However, federal changes in 1993 were not adopted until recently, so adjustments are generally necessary for new property that is non-residential rental property or Indian Reservation property, or for section 179 deductions that exceed \$13,000. And depreciation adjustments for property placed in service before 1987 are necessary because California still followed the federal pre-1981 depreciation methods up until 1987. As a result, the translation from the federal Form 4562 is a good starting point but is seldom the whole picture.

Multi-scheduling conforms to federal return. The IRS requires that a separate Form 4562 be completed for each separate business. The translation from the federal return therefore creates a separate Form 3885A for each separate copy of Form 4562 on the federal return. The automatic linking with the return matches the federal approach through the special California Worksheets A, C, E, F, and 4835. The copy number, the indication of the supported worksheet, and the business activity are therefore all automatically translated from the corresponding copy of Form 4562. By contrast, the FTB instructs filers to omit Form 3885A when the activity is passive and reported on Form 3801. Nevertheless, the detail on Form 3885A is required in support of Form 3801 entries, so we retain the form even when the adjustments are passed through Form 3801. (*CAUTION:* Although any federal Form 4562 associated with a federal Form 2106 is translated to the California Form 3885A, any adjustments resulting on that copy of Form 3885A are not posted anywhere automatically. You must enter any adjustments on the appropriate lines of the return, such as on Worksheet A or Schedule CA.)

CAUTION: View all worksheets after translation. Because the California format differs from the federal format, you **MUST** view all translated worksheets for Form 3885A to ensure their proper calculation and posting. Moreover, whenever you view ONE worksheet attached to a particular line, you must view ALL worksheets attached to the same line in order to ensure that all translated worksheets are included in the totals for the line.

Reshuffling of worksheets may be necessary. Because of the differences between California and federal formats, you may also need to remove some worksheets translated from the federal return and add others. The California form separates new (2004) property from all other property, and California law differed greatly from federal law before 1987. As a result there are three time periods into which we separate the form for data entry purposes: 2004 property, 1987 through 2003 property, and pre-1987 property. The federal form does not provide such a separation in some areas, however, so our translation of worksheets from the federal return may include translation of

some worksheets to the wrong groups. You may therefore have to remove some translated worksheets (by means of the Remove Key, shift-F3 or ctrl-R) and reenter their data in worksheets attached to other lines. Areas where this must be done include the following:

Section 168 Property. The worksheets attached to line 15 of the federal Form 4562 are translated to the Section 168 Worksheets for line 5 of the California form. However, the federal line can include property placed in service during 2004. The worksheets for 2004 property must be removed from line 5 and their data must be reentered on a Section 168 Worksheet for line 3.

50-year Property. The worksheets attached to the line above line 22 of the federal Form 4562 are translated to the MACRS/ACRS worksheets for line 5 of the California form. However, the federal line can include property placed in service during 2004. The worksheets for 2004 property must be removed from line 5 and their data must be reentered on MACRS/ACRS Worksheets for line 3.

Listed Property. The worksheets attached to lines 25 through 29 of the federal Form 4562 are translated to the MACRS/ACRS worksheets for line 5 of the California form. However, the federal lines 25 through 29 and their attached worksheets may include property placed in service during 2004 and property placed in service before 1987. Those Listed Property Worksheets must be removed from line 5; the 2004 data must then be reentered on MACRS/ACRS Worksheets for line 3, and the pre-1987 data must be reentered on Pre-87 Depreciation Worksheets for line 5.

Other depreciation. Similar procedures may be necessary for the federal "other depreciation" line above line 16 of federal Form 4562, but only rarely. This line is used almost exclusively for pre-1981 property on the federal return. But for the rare special cases of newer property (1987 or newer) where ACRS depreciation methods are not allowed on the federal return, you may have to remove the worksheets and reenter them elsewhere.

Altering of entries on some other worksheets may also be necessary. Even for worksheets that are already translated to the proper lines, you may have to alter some entries on the worksheets because of past differences between federal and California law.

Pre-1987 property. Adjustments are almost always required for property placed in service before 1987, when California had not yet conformed to federal ACRS methods.

Post-1992 property. Adjustments are often required for property placed in service in 1993 or later if section 179 deductions were claimed. The California ceiling remained at \$10,000 until 1997 while the federal ceiling rose to \$17,500 in that time; the California ceiling for 1997 was \$13,000 while the federal one was \$18,000; and the California ceiling for 1998 was \$16,000 while the federal one was \$18,500. (For 1999 both the California and federal ceilings were

\$19,000, for 2000 both were \$20,000, for 2001 and 2002 both were \$24,000, but for 2003 and 2004 the California ceiling is \$25,000 while the Federal ceiling is a whopping \$100,000 for 2003 and \$102,000 for 2004.)

Post-9/10/01 property. California has no provision analogous to the federal special 30% or 50% special depreciation allowance for new property. Since this special allowance is mandatory unless you elect out of it, an adjustment to the depreciation basis will now almost always be necessary.

Nonresidential real property after May 12, 1993, but before January 1, 1997. Finally, adjustments are also necessary for nonresidential real property placed in service on or after May 13, 1993, but before January 1, 1997, when the federal recovery period was increased from 31.5 years to 39 years while the California recovery period remained at 31.5 years.

PART I, IDENTIFY THE ACTIVITY AS PASSIVE OR NONPASSIVE. A single Form 3885A applies to a single activity, and so relates to either a passive or a nonpassive activity. When the activity is identified as passive, adjustments are passed through Form 3801 and eventually reflected in Schedule CA through lines labeled as PAL adjustments. But when the activity is identified as nonpassive, adjustments are passed directly through Schedule CA.

1 Completed for passive Activity? (auto-calc) The answer to the passive activity question is determined automatically based on your answers on the worksheet or schedule to which this copy of Form 3885A is attached. For an unattached copy or a copy for Schedule A, however, you may have to override the automatic entry.

Completed for nonpassive Activity? (auto-calc) Automatically the opposite of the above answer.

PART II, ELECTION TO EXPENSE CERTAIN TANGIBLE PROPERTY. California has an expensing provision similar to the federal provision for the year the property is first placed in service. However the California ceiling is only \$25,000 for 2004, in sharp contrast with the new federal ceiling of \$102,000.

FTB Sec. 179 Calculations. In order to determine the deductible amount for line 2 of Form 3885A, the FTB provides a worksheet in its instructions for Form 3885A which parallels the lines in Part I of federal Form 4562, but with different dollar limits and with qualified zone lines omitted. The worksheet appears on the screen, but you should refer to the instructions for Part I of Form 4562 that appear in Chapter 2 of the Tax Forms Guide 2005 Edition for details.

1 Maximum dollar limitation. (auto-calc) Normally \$25,000 for 2004.

MFS: cost of section 179 property for spouse. If married filing separately, your spouse's property also counts for line 2.

2 Total cost of sec 179 property placed during the tax year. (auto-calc) Computed as the total cost of assets for which you claim section

179 deductions at lines 6a (taken from your entries on the Section 179 Worksheets) and 6b (taken from your entries on the Listed Property Worksheets), plus, if married filing separately, all of the spouse's other Section 179 property.

- 3 Threshold cost before reduction in limitation.** *(auto-calc)* Automatically \$200,000.
- 4 Reduction in limitation.** *(auto-calc)* An excess cost is computed here as the total cost in line 2 less the threshold in line 3, but no less than zero.
- MFS: \$ deviation from 50/50 rule.** *(For MFS filing status ONLY.)* The dollar limitation is line 1 less line 4, but married taxpayers filing separately must split this amount between themselves. A 50/50 split is normal, but the FTB allows you to make a different split as long as the two of you deduct no more than the dollar limitation on both of your returns combined. This line is therefore provided to alter the split by allowing you to enter a dollar adjustment to the 50/50 split ranging from line 1 less line 4 to line 4 less line 1.
- 5 Dollar limitation for the tax year.** *(auto-calc)* Computed as line 1 less line 4, plus the preceding deviation if married filing separately, but no less than zero.
- 6 Other than listed property.** *(Supported by the Section 179 Worksheet.)* The claim for property placed in service in the current tax year is detailed here for all except listed property. The Section 179 Worksheets for this line are translated from the federal Section 179 Worksheets that support line 6 of federal Form 4562.
- 7 Listed property.** *(Supported by the Section 179 Worksheet.)* The claim for listed property is shown here. The Section 179 Worksheets for this line are translated from the federal Listed Property Worksheets that support lines 24 and 25 of federal Form 4562. All listed property worksheets are translated to this line, but only new property will have a section 179 deduction. You may therefore want to remove the extraneous worksheets with the Remove Key (shift-F3 or ctrl-R), but their presence will not affect the calculations for the return nor the official printouts for the FTB.
- 8 Total elected section 179 cost.** *(auto-calc)* Computed as line 6 plus line 7.
- 9 Tentative deduction.** *(auto-calc)* Computed as the lesser of line 5 or line 8. Limitations A and B on the second page of the Form 4562 section of Chapter 2 of the main Tax Forms Guide 2005 Edition are enforced here.
- 10 Carryover of disallowed deduction from 2003.** Enter here any amount of section 179 deduction disallowed on the California return in 2003 because of the limitation of the deduction to taxable business income.
- Adjustment to taxable income limitation.** The software takes into account all wages and self-employment income throughout the return,

but does not prorate it among separate Forms 4562. As a result, if you have more than one Form 3885A with Sec. 179 deductions, you will have to make a negative entry here to reduce the limitation on line 11 by the amount allocated to other Forms 3885A.

11 Taxable income limitation. *(auto-calc)* The limitation is applied here.

12 Section 179 expense deduction. *(auto-calc)* Computed as the lesser of line 11 or the sum of lines 9 and 10. This amount is carried to line 2 of Form 3885A, below.

13 Carryover of disallowed deduction to 2005. *(auto-calc)* Computed as line 0 plus line 10 less line 12, this is the amount disallowed due to the taxable income limitation on line 11, and can be used on next year's Form 3885A.

2 Amount from FTB worksheet. *(auto-calc)* Taken as line 12 of all the above FTB Sec. 179 Worksheets, this is the amount of the California deduction for section 179 expense. The adjustment relative to the federal amount is figured after line 8, because line 8 includes the federal Sec. 179 deduction in addition to all other depreciation.

PART III, DEPRECIATION. All depreciation other than the Section 179 deduction is figured here. The only details actually printed on the California Form 3885A are those for property newly placed in service in 2004. But the bulk of the calculations for the adjustments to be posted to Schedule CA apply to earlier years, especially before 1987, when California differed most appreciably from federal law. *CAUTION: California has not conformed to special provisions for qualified zone property nor Indian Reservation property.*

3 2004 California depreciation. *(Supported by the MACRS/ACRS Worksheet.)* These worksheets are translated from the worksheets for lines 19a through 20c of federal Form 4562, all of which are used solely for property newly placed in service in 2004. *CAUTION: If the lines on the federal Form 4562 for 50-year Property or Listed Property include property newly placed in service in 2004, you must remove those worksheets from the set at line 5 and reenter the data anew on the worksheets for THIS line.*

2004 California section 168 property. *(Supported by the Section 168(f)(1) Worksheet.)* No federal worksheets are translated to this line, so if any property reported on line 15 of the federal Form 4562 was placed in service in 2004, you must remove the corresponding Section 168 Worksheet that is translated to line 5 and reenter its data on a worksheet attached to this line.

2004 California listed property. *(Supported by the Listed Property Worksheet.)* No federal worksheets are translated to this line, so if any property reported on lines 25 through 29 of the federal Form 4562 was placed in service in 2004, you must remove the corresponding Listed Property Worksheet that is translated to line 5 and reenter its data on a worksheet attached to this line.

- 4 Add amounts on line 3, column (f).** *(auto-calc)* Computed as the sum of line (f) for the above depreciation worksheets, this is the total ONLY for newly placed property.
- 5 California depreciation for assets placed prior to 2004.** A number of separate sets of worksheets support this line because of differences between the federal and California forms and laws over the years. The data for most worksheets for property placed in service after 1986 or before 1993 will not need to be modified because of close conformance of California law to federal law. But see the preceding shaded areas for exceptions.
- Pre-2004 California section 168(f)(1) property.** *(Supported by the Section 168(f)(1) Worksheet.)* Translated from line 15 of federal Form 4562, including all worksheets attached to the line. You must modify the translated worksheets only to reflect past differences in the law. Be sure to remove worksheets from this line for any property newly placed in service in 2004, and reenter it in Sec. 168 Worksheets for line 3. (This line is reserved for property you elect on the federal return to depreciate by the units-of-production method or any other method not based on a term of years.)
- 1987 to 2003 California ACRS property.** *(Supported by the MACRS/ACRS Worksheet.)* Translated from line 17 of federal Form 4562. MACRS depreciation was allowed by California starting in 1987, so you will rarely have to modify the amounts translated to these worksheets from the federal Form 4562 unless you claimed section 179 deductions after 1992 or claimed depreciation for non-residential real property placed after May 12, 1993.
- Pre-1987 California ACRS property.** *(Supported by the Depreciation Worksheet for Pre-87 ACRS Property.)* Translated from the line two lines above line 16 of federal Form 4562. All ACRS Worksheets are translated to Depreciation Worksheets of the type described in the Tax Forms Guide for "Other depreciation" at line 16 of Form 4562 because California did not allow ACRS depreciation methods before 1987. For each worksheet you must adjust the basis, enter past depreciation claimed on the California return, and select the depreciation method you have used for the property on the California return in the past.
- Pre-2004 California other depreciation.** *(Supported by the Depreciation Worksheet.)* Translated from the line above line 16 of federal Form 4562. For this line, you must often alter the entries for all translated worksheets to reflect past differences in the law.
- 1987 to 2003 California listed property.** *(Supported by the Listed Property Worksheet.)* Translated from the worksheets that support lines 26 and 27 of federal Form 4562. MACRS depreciation was allowed by California starting in 1987, so you may not have to modify the amounts translated to these worksheets from the federal Form 4562 for post-1986 property. However, because California limita-

tions for section 179 deductions differed from federal limitations starting in 1993, you may have to change the depreciation basis for these properties. CAUTION: Because the federal form reports both new and old listed property on the same line, some worksheets for pre-1987 property may be translated to this line. The results for those worksheets will be automatically zeroed when you view the supporting pages, but you will have to reenter the data on the worksheets for the proper lines.

Pre-1987 listed property. *(Supported by the Depreciation Worksheet for Pre-87 Listed Property.)* The data for any Listed Property Worksheets, above, that is zeroed because it is for post-1986 property must be reentered on these worksheets. For each worksheet page for pre-1987 property you must adjust the basis as necessary, enter past depreciation claimed on the California return, and select the depreciation method you have used for the property on the California return in the past.

5 California depreciation for assets placed prior to 2004. *(auto-calc)* Computed as the results from all of the above worksheets.

6 Total California depreciation. *(auto-calc)* Computed as the sum of lines 2, 4, and 5.

7 Total federal depreciation. Translated from line 22 of federal Form 4562.

8 Depreciation adjustment. *(auto-calc lines)* Line 8a is computed as line 6 less line 7, but no less than zero, and line 8b is computed as line 7 less line 6, but no less than zero. Note that these adjustments are *NOT* necessarily posted directly to Schedule CA because of the involvement of Form 3801 for passive activities.

PART IV, AMORTIZATION. The amortization adjustment is nominally determined by comparing the deductions claimed in the following worksheet with those claimed on the federal form:

9 2004 amortization. *(Supported by the Amortization Worksheet.)* This line is translated from line 42 of federal Form 4562, which is used for reporting the amortization of 2004 property.

10 Total California amortization. *(auto-calc)* Computed as the sum of line (f) for all above amortization worksheets, this is the total ONLY for newly placed property.

11 California amortization for property placed before 2004. *(Supported by the Amortization Worksheet.)* This line is translated from line 43 of federal Form 4562, which is used for reporting the amortization of pre-2004 property. Several particulars of the California law differ from the federal law, especially for amortization initiated several years ago, so the worksheet entries transferred from the federal return may have to be altered.

12 Total California amortization. *(auto-calc)* Computed as the sum of lines 10 and 11.

13 Total federal amortization. Translated from total amortization at line 44 of federal Form 4562.

14 Amortization adjustment. (*auto-calc*) Line 14a is computed as line 12 less line 13, but no less than zero. Line 14b is computed as line 13 less line 12, but no less than zero. Note that these adjustments are NOT necessarily posted directly to Schedule CA because of the involvement of Form 3801 for passive activities.

Allocation to Schedule CA. The net adjustment from all activities is the sum of lines 8a and 14a less the sum of lines 8b and 14b from both the nonpassive and passive sections. Worksheets A, C, E, F, and 4835 are used to collect all adjustments from Form 3885A, then the nonpassive parts are posted directly to Schedule CA, which those worksheets support through the Road Map. The passive parts are passed through Form 3801 before separate posting to Schedule CA.

***Form 5123 / Employer-Provided Adoption Assistance Exclusion**

Purpose. This form, which is analagous to a small portion of federal Form 8839, is used to figure an exclusion from income of employer-provided adoption benefits you received.

*** Included in Premium Level software ONLY.** This form is only built into the Premium Level version of the California Supplement. It is detailed in the separate *Premium Level Supplement 2005*. (When available, Form 5123 is accessible only through the Forms Menu and not through the Road Map.)

Form 5805/5805-F / Underpayment of Estimated Tax

HINT: It may be advisable NOT to file Form 5805. Thanks to an offer from the FTB, there is a strong impetus for not filing this form yourself. If you file Form 5805 and compute the penalty yourself, you must pay the penalty with the return; but if you let the FTB compute the penalty, you do NOT have to pay the penalty when you file, but only when the FTB bills you. Nevertheless, we provide the form with its full automation so that taxpayers are not caught unaware of a penalty they may owe.

Automatically generated. Note that a California Form 5805 is automatically created during translation if a federal Form 2210 was completed. You may not need to file this form, however, if there is no question of a penalty, and you may therefore have to remove the form from the California return. If no Form 2210 existed on the federal return, but you may be subject to a penalty on the California return, Form 5805 will be automatically generated and completed based on the information available on Form 540 (unless you specified on the Control Form the blocking of the auto-creation of Form 5805).

***CAUTION:** In order for the automated Form 5805 to take into consideration the special exceptions that are based on 2003 amounts, you must supply the information from the 2003 California return that is requested on screen 1 of the Control Form.*

Farmers and fishermen get an extra break. Like federal Form 2210-F, qualifying farmers and fishermen can use Form 5805-F to compute the penalty rather than Form 5805. It provides more exceptions, and an ability to avoid all late-payment penalties if you file and pay all tax due by March 1, 2005. And, like Form 2210-F, Form 5805-F is built into the software and automatically used in place of Form 5805 when applicable.

Fully automatic unless you qualify for a special exception. The form is automatically completed and computed based on the withholding and estimated tax payments reported on Form 540. If you qualify for an exception based on your prior-year tax return, however, you must enter the additional information on the Control Form and Form 5805 to benefit from the exception. In addition, like the federal Form 2210, the software assumes that late payments are made on the next due date, not on some intermediate date, so you may have to override the computations if you make payments on other dates.

EXCEPTIONS. The exceptions that are unique to a California return are described here, because there is no parallel on the federal Form 2210. If you qualify for any of these exceptions, no penalty is computed.

Full 12 months for 2003 included below? (*auto-calc*) If you supplied 2003 information on screen 1 of the Control Form and answered Yes to the corresponding question that appears there, a Yes will appear here and 2003 amounts will be considered in the following exceptions. Otherwise the worst

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Form 5805/5805-F

case is assumed: that you do not qualify for any reduction in payment requirements based in your 2003 tax.

1 Were you required to pay LESS than \$200 (\$100 if MFS) with either your 2003 OR 2004 tax return? If so, you qualify for an exception.

a For 2004: Form 540, line 34 less G-1 tax. *(auto-calc)* Taken from Form 540 as indicated.

b 2004 Form 540 lines 38, 40, and 41. *(auto-calc)* Taken from Form 540 as indicated.

c Subtract line b from line a. *(auto-calc)* Computed as indicated.

Qualify for 2004 exception 1. *(auto-calc)* If line c is less than \$100 (\$50 if married filing separately), you qualify and the penalty on Form 5805 will be zero.

d For 2003: Form 540, line 34 less G-1 tax. *(auto-calc)* Taken from the entry on screen 1 of the Control Form.

e 2003 Form 540 lines 38 and 41. *(auto-calc)* Taken from the entries on screen 1 of the Control Form.

f Subtract line e from line d. *(auto-calc)* Computed as indicated.

Qualify for 2003 exception 1. *(auto-calc)* If line f is less than \$100 (\$50 if married filing separately), you qualify and the penalty on Form 5805 will be zero.

2 Your 2003 return was for a full 12 months and you did not have any tax liability on that return? If so, you qualify for an exception.

a For 2003: Form 540 line 34 less G-1 tax. *(auto-calc)* Taken from the entries on screen 1 of the Control Form.

Qualify for exception 2. *(auto-calc)* You qualify if the above amount is zero AND you answered Yes to "2003 amounts entered for Form 5805" on the Control Form, and the penalty on Form 5805 will then be zero.

3 Were 2004 estimated tax plus withholding payments at least 90% of 2004 tax or 100% of 2003 tax liability (110% if 2003 AGI was more than \$150,000, \$75,000 if married filing separately)? If so, you may qualify for an exception, but further requirements apply as noted below.

2004 tax paid in required installments? You cannot qualify for the exception unless you can answer Yes.

a 2004 Form 540 lines 38, 40, 41, and estimated tax payments in 39. *(auto-calc)* Taken from Form 540 lines 38 through 41, but excluding the amount in line 39 that is paid with a filing extension.

b Tax on 2004 Form 540, line 34 less G-1 tax. *(auto-calc)* Taken from Form 540 as indicated.

c Divide line a by line b. *(auto-calc)* Computed as indicated.

Qualify for 2004 exception 3. *(auto-calc)* You qualify if line c is at least 0.9.

d Tax on 2003 Form 540, line 34 less G-1 tax. *(auto-calc)* Taken from the entries on screen 1 of the Control Form.

e Divide line a by line d. *(auto-calc)* Computed as indicated, but no more than 1.1.

Qualify for 2003 exception 3. *(auto-calc)* You qualify if line e is one or more (1.1 or more if 2003 AGI was more than \$150,000, or \$75,000 if married filing separately).

Remainder of form parallels federal Form 2210. The remaining parts of the basic Form 5805 parallel federal Form 2210, including Form 2210-F for farmers and fishermen, although certain percentages differ. The Annualized Method portion of Form 5805 also parallels corresponding portion of federal Form 2210, except for the omission of a self-employment section. You should therefore consult the detailed instructions for Form 2210 in Chapter 2 of the Tax Forms Guide 2005 Edition for additional help.

***Form 5870A / Tax on Accumulation Distribution of Trusts**

Purpose. This form, which is analagous to federal Form 4970, is used to figure the additional tax on an accumulation distribution made by a foreign trust and certain domestic trusts.

*** Included in Premium Level software ONLY.** This form is only built into the Premium Level version of the California Supplement. It is detailed in the separate *Premium Level Supplement 2005*. (When available, Form 5870A is accessible through the Road Map at line 23 of Form 540.)

Worksheet A / Itemized Deductions

Collects adjustments to federal Schedule A. This worksheet is not an FTB form or schedule but is built into the software to make the automation of the return complete. It collects relevant data from federal Schedule A and the copy of California Form 3885A (Depreciation and Amortization Adjustment) that relates to Federal Schedule A, then allocates the results to the proper adjustment lines on Schedule CA (California Adjustments Schedule). Several of the amounts shown here are also used in Part I of California Schedule P (adjustments and preferences for AMT). The worksheet is printed as a part of the return in support of the entries that appear on Schedule CA.

MEDICAL AND DENTAL EXPENSE. Adjustments to line 4 of federal Schedule A are handled here. In this and all subsequent sections, the line flagged by an arrow is the resulting California itemized deduction for each section.

Amount on federal Schedule A, line 1. Translated as indicated, this is the amount of medical and dental expenses reported on the federal return before limitation to the amount that exceeds 7.5% of AGI.

California adjustment to federal Schedule A, line 1. Most taxpayers would have no adjustment, but California treats a registered domestic partner as your spouse. As a result, you may have an adjustment here if you have a registered domestic partner. For example, health insurance paid on behalf of the partner is a valid expense. However, do not include any insurance you claimed at line 31 of Schedule CA.

Federal Schedule A, line 1 using California amounts. *(auto-calc)* Computed as the amount on federal Schedule A, line 1, plus the preceding adjustment.

Amount on Federal Schedule A, line 2. *(auto-calc)* Taken from line 13 of Form 540, this is the federal AGI for the return.

Amount on Federal Schedule A, line 3. *(auto-calc)* Computed as 7.5% of the preceding line, this is the floor below which no medical expenses are deductible. California conforms fully with this limitation, including the use of federal AGI rather than California AGI.

➔ **Federal Schedule A, line 4 using California amounts.** *(auto-calc)* Computed as the amount by which "Federal Schedule A, line 1 using California amounts" exceeds the preceding floor.

Amount on federal Schedule A, line 4. Translated as indicated, this is the net amount of medical and dental expenses claimed on the federal return after applying the AGI-related limitation.

California adjustment to federal Schedule A, line 4. *(auto-calc)* Computed as "Federal Schedule A, line 4 using California amounts" less the amount on the preceding line.

TAXES YOU PAID. Adjustments to line 9 of federal Schedule A are handled here.

Amount on federal Schedule A, line 9. Translated as indicated, this is the total tax deducted on federal Schedule A.

State/local taxes on federal Schedule A, line 5. Translated from federal Schedule A as indicated, this is state and local income or sales tax deducted on the federal return, including state disability insurance (SDI).

1099 foreign taxes included in federal Schedule A, line 8. Translated from the line "1099 foreign inc tax in A, ln 8" on our federal Schedule A, this is the foreign tax elected to be deducted on Schedule A rather than claimed on Form 1116.

Other foreign income taxes included in federal Schedule A, line 8. Translated from the line "Other foreign inc tax in A, ln 8" on our federal Schedule A, this is all other foreign tax claimed as an itemized deduction on the federal return.

Other nondeductible taxes included in line 8. Translated from the line "Other fed-deductible" on our federal Schedule A, this is the part of line 8 identified on the federal return as deductible *ONLY* on the federal return (other than the preceding foreign taxes).

California adjustment to federal Schedule A, line 9. *(auto-calc)* Computed as the negative of the sum of the preceding four taxes from federal Schedule A, and reflected in Schedule CA line 38.

→ **Federal Schedule A, line 9 using California amounts.** *(auto-calc)* Computed as "Amount on federal Schedule A, line 9" plus the preceding adjustment.

INTEREST YOU PAID. Adjustments to line 14 of federal Schedule A are handled here.

Amount on federal Schedule A, line 13. Translated as indicated, this is the investment interest deducted on federal Schedule A.

Investment interest adjustment on California Form 3526. *(Road Map line for Premium Level software, supported by Form 3526.)* The difference between investment interest claimed on federal Form 4952 and investment interest claimed on California Form 3526 is reported here.

Federal Schedule A, line 13 using California amounts. *(auto-calc)* Computed as "Amount on federal Schedule A, line 13" plus the preceding adjustment.

Amount on federal Schedule A, line 14. Translated as indicated, this is the total interest deducted on federal Schedule A.

Mortgage interest credit on federal Form 8396. Translated from the line above line 10 of the federal Schedule A, this is mortgage interest credit on IRS Form 8396 that reduced your federal itemized deductions at line 10 of Schedule A.

Investment interest adjustment from California Form 3526. *(auto-calc)* Taken from the earlier line that has the same label, this is the part

of the adjustment to Schedule A, line 14 that stems from Schedule A, line 13.

Other interest adjustment. Enter any other interest adjustment here. An example of interest reportable here but not deductible on the federal return is interest you paid on a loan from a utility company used to pay for energy-efficient products for California residences.

California adjustment to federal Schedule A, line 14. *(auto-calc)* Computed as the sum of the preceding three adjustments.

- ➔ **Federal Schedule A, line 14 using California amounts.** *(auto-calc)* Computed as "Amount on federal Schedule A, line 14" plus the preceding adjustment.

GIFTS TO CHARITY. Adjustments to line 18 of federal Schedule A are handled here.

Amount on federal Schedule A, line 15. Translated from the federal return as indicated, these are the contributions made by cash or check.

Amount on federal Schedule A, line 16. Translated from the federal return as indicated, these are the noncash contributions.

California carryover from prior year. Enter the carryover from prior years. This line is *NOT* translated from the federal return because federal and California limitations differed substantially before the California Tax Reform Act, so the carryovers are almost always different.

Maximum contribution by federal law. *(auto-calc)* Computed as 50% of the federal AGI on line 13 of Form 540.

- ➔ **Federal Schedule A, line 18 using California amounts.** *(auto-calc)* Computed as the sum of federal lines 15 and 16 plus the California carryover, but no more than the maximum contribution by federal law.

Amount on Federal Schedule A, line 18. Translated from the federal Schedule A as indicated, this is the net deduction claimed for contributions to charities on the federal return.

California adjustment to federal Schedule A, line 18. *(auto-calc)* Computed as "Federal Schedule A, line 18 using California amounts" less the preceding federal deduction.

CASUALTY AND THEFT LOSSES. Adjustments to line 19 of federal Schedule A are handled here.

Amount on federal Schedule A, line 19. Translated as indicated, this the amount of casualty and theft loss claim on the federal return through Form 4684.

California adjustment to federal Schedule A, line 19. Most taxpayers would have no adjustment, but differences could arise if the basis of the property lost is different under California rules.

- ➔ **Federal Schedule A, line 19 using California amounts.** *(auto-calc)*
Computed as "Amount on federal Schedule A, line 19" plus the preceding adjustment.

JOB EXPENSE AND MOST OTHER. Depreciation, amortization, and other adjustments to line 26 of federal Schedule A are handled here.

Amount on federal Schedule A, line 23. Translated from the federal Schedule A as indicated, this is the federal deduction before limitation to the amount that exceeds 2% of AGI.

Form 4684 deduction in federal Schedule A, line 27. Translated from the federal Schedule A as indicated, this amount is subject to the 2% of AGI floor on the California return even though it is not on the federal return.

Depreciation adjustment (Form 3885A). *(Road Map line, supported by Form 3885A.)* The copy of Form 4562 that is attached to federal Schedule A is translated to Form 3885A and attached to California Worksheet A. The amount on that appears here relates to the depreciation and amortization deductions included in line 22 of federal Schedule A.

Other adjustments to federal Schedule A, line 23. Enter any other adjustments here, such as adjustments for employee business expenses and nontaxable income expenses. You will have an adjustment for employee business expenses if the car depreciation you used on federal Form 2106 is different by California rules, which is likely for cars placed in service before 1987. You will have a positive adjustment for nontaxable income expenses if you failed to deduct on federal Schedule A expenses related to producing income that is taxable by California law but not by federal law. You will have a negative adjustment for nontaxable income expenses if you deducted on federal Schedule A expenses related to producing income that is taxable by federal law but not by California law. If any entries here come from a refigured amount from Form 2106, you must attach to the California return a copy of Form 2106 with the modified amounts.

California adjustment to federal Schedule A, line 23. *(auto-calc)* Computed as the sum of the preceding three lines.

Federal Schedule A, line 23 using California amounts. *(auto-calc)*
Computed as "Amount on federal Schedule A, line 23" plus the preceding adjustment.

Amount on federal Schedule A, line 24. *(auto-calc)* Taken from line 13 of Form 540, this is the federal AGI for the return.

Amount on Federal Schedule A, line 25. *(auto-calc)* Computed as 2% of the AGI on the preceding line, this is the floor below which no expenses in this section are deductible. California conforms fully with this limitation, including the use of federal AGI rather than California AGI.

- ➔ **Federal Schedule A, line 26 using California amounts.** *(auto-calc)*
Computed as the amount by which "Federal Schedule A, line 23 using California amounts" exceeds the amount on the preceding line.
- Amount on federal Schedule A, line 26.** Translated from the federal Schedule A as indicated.
- California adjustment to federal Schedule A, line 26.** *(auto-calc)* Computed as "Federal Schedule A, line 26 using California amounts" less the preceding amount.

MISCELLANEOUS DEDUCTIONS. Adjustments to line 27 of federal Schedule A are handled here.

- Gambling losses in federal Schedule A, line 27.** Translated from the "Gambling losses" line on our federal Schedule A.
- California lottery losses.** Enter here any gambling losses in the above that stem from the California lottery. These losses are *NOT* deductible on the California return.
- California lottery loss adjustment.** *(auto-calc)* Computed as the negative of the preceding amount.
- Other adjustment to gambling losses.** Enter any other adjustment here.
- California adjustment to gambling.** *(auto-calc)* Computed as the sum of "California lottery loss adjustment" and the preceding amount.
- California-allowed gambling loss.** *(auto-calc)* Computed as "Gambling losses in federal Schedule A, line 17" plus the preceding adjustment.
- Amount on federal Schedule A, line 27.** Translated from the federal Schedule A as indicated, this is the total miscellaneous deductions claimed on the federal Schedule A that are not subject to the 2%-of-AGI floor.
- California gambling adjustment to federal Schedule A, line 27.** *(auto-calc)* Taken from the previously-computed "California adjustment to gambling."
- California Form 4684 adjustment to federal Schedule A, line 27.** *(auto-calc)* Computed as the negative of the amount from federal Form 4684 that was added to the preceding section (JOB EXPENSE AND MOST OTHER). This amount is subject to the 2%-of-AGI floor on a California return.
- Other adjustment to federal Schedule A, line 27.** Enter any other miscellaneous adjustments here.
- California adjustment to federal Schedule A, line 27.** *(auto-calc)* Computed as the sum of the preceding three adjustments.
- ➔ **Federal Schedule A, line 27 using California amounts.** *(auto-calc)*
Computed as "Amount on federal Schedule A, line 27" plus the preceding adjustment.

ALLOCATION TO SCHEDULE CA. (*auto-calc lines*) The adjustments in the preceding sections are summarized here.

FEDERAL DEDUCTIONS FOR SCHEDULE CA, LINE 37. (*auto-calc*)

Computed as the sum of the amounts on federal Schedule A lines 4, 9, 13, 18, 19, 26, and 27, each of which is shown in one of the preceding seven sections. This is the total federal itemized deduction claimed before the limitation for high AGI was imposed.

TOTAL ADJUSTMENT FOR SCHEDULE CA, LINE 38. (*auto-calc*)

Taken as the "California adjustment to federal Schedule A, line 9," but expressed as a positive number, this is the amount of taxes that were deducted on the federal return but are not deductible on the California return. They are subtracted from the federal deductions at line 39 of Schedule CA.

TOTAL ADJUSTMENT FOR SCHEDULE CA, LINE 40. (*auto-calc*)

Computed as the sum of California adjustments for federal Schedule A lines 4, 9, 13, 18, 19, 26, and 27, each of which is shown in one of the preceding seven sections. This is the net adjustment to the federal deductions excluding the adjustment for taxes (which is applied separately via line 38 of Schedule CA).

For Itemized Deductions Worksheet for Schedule CA, line 42:

California amounts for lines 4, 14, 19, and gambling part of 27. (*auto-calc*) Computed as indicated, as shown in the preceding sections, this amount is used in the indicated worksheet to determine the amount for Schedule CA, line 42 after the phaseout for high AGI is applied.

Extra line for personal memos. Provided for supporting statements that will not be printed with the official return.

Worksheet B / Interest and Dividends

Collects adjustments to federal Schedule B. This worksheet is not an FTB form or schedule but is built into the software to make the automation of the return complete. It collects relevant data on federal Schedule B and computes adjustments for California Schedule CA based on amounts that are taxed differently on federal and California returns.

INTEREST. Adjustments to interest reported on federal Schedule B are computed here.

Taxable interest on federal Schedule B. The total on line 4 of federal Schedule B is translated to this line, which is posted to Schedule CA, line 8, column A.

U. S. Savings Bonds on federal Schedule B, line 2. The indicated amount is translated from the federal Schedule B line labeled "US Savings bonds, etc," which is identified on the 1099-INT worksheets. California DOES NOT tax interest on bonds or obligations of the U. S. or its territories, even though the federal government does.

Bonds excluded on federal Schedule B, line 3. The indicated amount is translated from the indicated line of federal Schedule B. It is the part of the preceding amount that is NOT included in federal AGI.

U. S. Savings Bonds in federal AGI. (*auto-calc*) Computed as the total U. S. Savings Bond amount less the preceding exclusion.

Other amounts taxed by federal but not California. Enter here any other U. S. obligations that are included in line 2 of the federal Schedule B. Be sure to include tax-free interest passed through to you through S corporations, partnerships, and trusts, which are taxed on the federal return. Do not include, however, amounts that are taxable by California, such as all interest from FNMA bonds, GNMA bonds, and FHLMC securities.

Interest subtraction. (*auto-calc*) Computed as the U. S. Savings Bonds in federal AGI plus the preceding entry, this result is posted to Schedule CA, line 8, column B.

California taxable amount included in Form 1040 line 8b. The indicated amount is translated from the federal Schedule B line labeled "Taxable ONLY by state," which is identified on the 1099-INT worksheets. California DOES tax interest on state and municipal bonds or obligations issued by other states or localities within other states, including the District of Columbia.

Other amounts taxed by California but not federal. Enter here any interest from other non-California government obligations not included in federal AGI.

Interest addition. (*auto-calc*) Computed as the California taxable amount in 1040 line 8b plus the preceding entry, this result is posted to Schedule CA, line 8, column C.

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Worksheet B

DIVIDENDS. Adjustments to dividends reported on federal Schedule B are computed here.

Taxable dividends on federal Schedule B. The total on line 6 of federal Schedule B is translated to this line, which is posted to Schedule CA, line 9, column A.

Dividends taxable on federal return but not California return. Any amount you enter here is posted to Schedule CA, line 9, column B.

Dividends taxable on California return but not federal return. Any amount you enter here is posted to Schedule CA, line 9, column C.

Extra line for personal memos. Provided for supporting statements that will not be printed with the official return.

Worksheet C / Business Income

Collects adjustments to federal Schedule C. This worksheet is not an FTB form or schedule but is built into the software to make the automation of the return complete. It collects relevant data on each federal Schedule C and the results from Form 3801 (Passive Activity Loss Limitations) and Form 3885A (Depreciation and Amortization Adjustment), then allocates the results to the proper adjustment lines on Schedule CA (California Adjustments Schedule). Form 3801 and the copy of Form 3885A that is attached to this worksheet are accessible through Road Map lines on this worksheet. The worksheet is printed as a part of the return in support of the entries that appear on Schedule CA.

Fully automatic for a translated return. All lines on this worksheet are either translated lines, Road Map lines, or Auto-calc lines. As a result no manual entries are required. (See the details for federal Schedule C in Chapter 2 of the main Tax Forms Guide 2005 Edition.)

CAUTION: Federal business code required on this worksheet. This entry (on screen 1 of Schedule C) is translated from your entry for the federal Principal Business Activity (PBA) Code on line B of the federal Schedule C. The 6-digit number on this line for copy 1 of Worksheet C is printed along with the taxpayer name and address at the top of Form 540. Reporting the PBA number to the FTB *is now mandatory*. The FTB is authorized to disclose this PBA code, along with other personal information like SSN and address, to city tax officials under specific limited circumstances. *CAUTION: If you will print using Laser-graphic or Window-graphic forms, you must make sure that the 6-digit code that appears here contains no spaces so that the code is printed in the proper format for the scannable Form 540.* Spaces are appropriate only for a manually completed Form 540, in which you use the FTB form with hand-print boxes.

Worksheet E / Supplemental Income

Collects adjustments to federal Schedule E. This worksheet is not an FTB form or schedule but is built into the software to make the automation of the return complete. It collects relevant data on federal Schedule E and the results from Form 3801 (Passive Activity Loss Limitations) and Form 3885A (Depreciation and Amortization Adjustment), then allocates the results to the proper adjustment lines on Schedule CA (California Adjustments Schedule). Form 3801 and the copy of Form 3885A that is attached to this worksheet are accessible through Road Map lines on this worksheet. The worksheet is printed as a part of the return in support of the entries that appear on Schedule CA. (See the details for federal Schedule E in Chapter 2 of the main Tax Forms Guide 2005 Edition.)

Additional entries may be required. Although the form is automatically completed from translated lines and Road Map lines, further adjustment may be necessary; not all required information is available on the federal return, and amounts reported to you (from partnerships, etc.) on California Schedules K-1 may be different from amounts reported to you on federal Schedules K-1.

Part I, Rental Property. The allocation of rental property income and loss for federal Form 8582 does not separately reflect the allocation for the depreciation part of the income or loss. As a result, if you have an adjustment for depreciation for your rental properties (on the Form 3885A that is attached to this worksheet), you must alter the translated amounts destined to Form 3801 yourself to reflect the adjustment. When you fail to do so, a nonzero amount will appear on one of the lines labeled "ERROR in above gain allocation" or "ERROR in above loss allocation." Unless the ERROR is zero, the accuracy of Form 3801 cannot be assured.

Parts II and III, Partnerships, etc. Adjustments to the entries translated from the federal return are necessary in these two sections when the amounts reported to you on California Schedules K-1 are different from those reported to you on federal Schedules K-1. *All Partnership and Estates/Trusts Worksheets from the federal return are translated*, so only the K-1 lines need be changed. The losses disallowed from Form 3801 are computed automatically and reflected in the results for this section.

Part IV, Farm Rental Income. (*Road Map lines, supported by Worksheet 4835.*) Adjustments to Form 4835 are performed on the supporting worksheet, not here. The results are reported here rather than directly on Schedule CA only because the results for federal Form 4835 are reported on federal Schedule E. All adjustments on Worksheet 4835 are passed through Schedule E without modification.

Allocation to Schedule CA. The allocation of adjustments from all sections to Schedule CA is fully automatic. Amounts are separated into passive and nonpassive parts to ensure the proper automation of the return.

Worksheet F / Farm Income

Collects adjustments to federal Schedule F. This worksheet is not an FTB form or schedule but is built into the software to make the automation of the return complete. It collects relevant data on each federal Schedule F and the results from Form 3801 (Passive Activity Loss Limitations) and Form 3885A (Depreciation and Amortization Adjustment), then allocates the results to the proper adjustment lines on Schedule CA (California Adjustments Schedule). Form 3801 and the copy of Form 3885A that is attached to this worksheet are accessible through Road Map lines on this worksheet. The worksheet is printed as a part of the return in support of the entries that appear on Schedule CA.

Fully automatic for a translated return. All lines on this worksheet are either translated lines, Road Map lines, or Auto-calc lines. As a result no manual entries are required. See the details for federal Schedule F in Chapter 2 of the regular Tax Forms Guide 2005 Edition.

Worksheet 4835 / Farm Rental Income

Collects adjustments to federal Form 4835. This worksheet is not an FTB form or schedule but is built into the software to make the automation of the return complete. It collects relevant data on federal Form 4835 and the results from Form 3801 (Passive Activity Loss Limitations) and Form 3885A (Depreciation and Amortization Adjustment), then allocates the results to the proper adjustment lines on Worksheet E. The adjustments then make their way to Schedule CA (California Adjustments Schedule) through Schedule E. Form 3801 and the copy of Form 3885A that is attached to this worksheet are accessible through Road Map lines on this worksheet. The worksheet is printed as a part of the return in support of the entries that appear on Schedule E and Schedule CA.

Fully automatic for most taxpayers for a translated return. Except for two lines for California adjustment, this worksheet is comprised of translated lines, Road Map lines, or Auto-calc lines. As a result only the adjustment lines may require your manual entry. See the details for federal Form 4835 in Chapter 2 of the regular Tax Forms Guide 2005 Edition.

Form 540-ES / Estimated Tax Worksheet

Parallels federal Form 1040-ES. The operation of this form parallels the operation of federal Form 1040-ES, so it is not separately detailed here. For most taxpayers the completion of the form will be fully automatic, based on expected changes translated from the federal Form 1040-ES and automatic transfers from the California Form 540. See the section for federal Form 1040-ES in Chapter 2 of the main Tax Forms Guide 2005 Edition for details.

Form 540X / Amended Individual Income Tax Return

Operates like federal Form 1040X. The operation of this form closely parallels the operation of federal Form 1040X, so it is not separately detailed here. If you first create the form before you modify the return that you filed, Form 540X will be complete once you complete the Form 540 return. You will need to access Form 540X only if you need to supply supporting detail for any of the changes. See the section for federal Form 1040X in Chapter 2 of the main Tax Forms Guide 2005 Edition for details.

Form 8453 / Declaration for Electronic Filing

Operates like federal Form 8453. *(Available only for Standard and Premium Level.)* The Form 8453 for the California return operates similarly to Form 8453 for the federal return, but the details are different. While its entries are translated from the federal Form 8453, one visible difference is that the worksheets for Forms W-2, W-2G, and 1099-R are accessible here, whereas they are accessible only from Form 1040 on the federal return. *If you have to make a correction to Form W-2, W-2G, or 1099-R for a California e-file return, this is where you must do it. The worksheets attached to Form 540 are used for calculations only and are not transmitted with the return.* Everything else on California Form 8453 is similar to federal Form 8453, including the preliminary checks for eligibility for electronic filing, which are slightly different for California. See FTB Publication 1345 for the rules on the checks that are automated here. See the section for federal Form 8453 in Chapter 2 of the main Tax Forms Guide 2005 Edition for all other details.

Form 8454 / e-file Opt-Out Record

For recording reason a return was not e-filed. *(Available only for Standard and Premium Level.)* Paid preparers who prepared more than 100 Form 540 returns for tax year 2003 are required to e-file all eligible Form 540 returns for 2004. However, taxpayers can choose *not* to have their return e-filed by signing Form 8454 for the preparer's records. The preparer can also choose not to e-file a return for "reasonable cause," which is also recorded on Form 8454. The preparer is required to retain the form for potential audit by the IRS but is instructed *not* to file it with any return.