



State and Local Tax Alert

October 2008

Major Changes to California Tax Law Impacting You

The recently approved California Budget features substantial changes to California tax laws impacting individuals and businesses. Most are designed to accelerate cash-flow to the state in order to mitigate the impact of the budget deficit. These changes include:

- **Suspension of the net operating loss (NOL) carryforward deduction**
- **Limitations on the use of tax credits**
- **Acceleration of estimated tax payments**
- **Elimination of the “prior-year’s tax” safe harbor estimated payment provisions for high income individual taxpayers**
- **Acceleration of the annual LLC fee**
- **Repeal of use tax exemption for vehicles and aircraft**

Suspension of net operating losses and other changes to NOL rules

Taxpayers with taxable income over \$500,000 will have their net operating loss deductions suspended for tax years 2008 and 2009. Beginning in 2008, the carryforward period for NOLs is extended from 10 to 20 years. Beginning in 2011, taxpayers will be permitted to carry back NOLs for two years. Carrybacks will be limited to 50% of NOLs for 2011 and 75% for 2012. Full NOL carrybacks will be allowed beginning in 2013.

Limitations on the use of tax credits

For tax years 2008 and 2009, utilization of tax credits for taxpayers with incomes of \$500,000 or more is limited to 50% of the tax liability reflected on the return. Other taxpayer-friendly changes in the credit rules will allow corporations to share credits within a single group if the receiving member was in the group when the credit was earned (formerly the credit could only be utilized by the generating member).

SJ Commentary: Impact on remaining 2008 estimated payments

The suspension of net operating losses and limitations on credit utilization, beginning this year, may impact corporate and individual estimated payments. Currently, there is no guidance or commentary from the Franchise Tax Board (FTB) regarding interest and penalties for underpayments in the first three quarters. Presumably, taxpayers will be allowed a grace period for

underpayments occurring as a result of the new rules. It may be prudent for taxpayers and tax practitioners to adjust 2008 fourth quarter estimates to take into account the new NOL suspension and credit limitation rules.

Estimated tax payment changes

Beginning in 2009, corporations and individuals will be required to submit 30% of their estimated liability in both quarters one and two, and 20% in each third and fourth quarter installment.

Elimination of estimated payment penalty safe harbor

For individual taxpayers with adjusted gross income of \$1 million or more (\$500,000 for single taxpayers), the safe harbor estimated tax rule based on the prior year's liability is eliminated. High income taxpayers will now need to submit estimates based on the current year's income projections.

Acceleration of annual limited liability company (LLC) fee

Effective for 2009, the annual LLC fee based on gross receipts will be due on the 15th day of the sixth month of the tax year. Formerly, payments were due on the 15th day of the fourth month following the close of the tax year.

Repeal of use tax exemption for vehicle and aircraft purchases

The 90-day, out-of-state exemption for vehicle and aircraft purchases has been changed to 12 months. California residents are required to keep their vehicles and aircraft out of California for 12 months to qualify or meet the criteria for other exemptions. This change is now permanent; a previous modification to the law was temporary.

For more information or if you have questions, please contact Tim Barnthouse, Principal – State and Local Tax, at (949) 777-1207, or call any professional on your Stonefield Josephson client service team.



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