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Taxation

Personal Income Tax; penalties

Revenue and Taxation Code §18684.2 (new).
AB 710; STATS 1970, Ch 506
(Effective July 24, 1970)

Section 18684.2 now added, provides that if there is a failure to pay the full amount of tax on or before the date prescribed for payment of such tax there will be a penalty of: (1) 5 percent of the total unpaid tax and (2) an amount computed at the rate of 0.5 percent per each month of the remaining tax, not to exceed 36 months. This Section is not to apply if the taxpayer can show that the failure was due to a reasonable cause and not due to willful neglect.

For purposes of this Section, total unpaid tax is defined as the amount of tax shown on the return reduced by: (1) the amount of any part of the tax which is paid on or before the date prescribed for filing the return, and (2) the amount of any credit against the tax which may be claimed on the return. Remaining tax is defined as the total unpaid tax reduced by the amount (if any) of any payment of the tax.

The penalties described above shall not apply if the sum of the penalties described above are less than the sum of the penalties imposed under Sections 18681 and 18682 which prescribe for the addition of 5% of the tax added for each month or fraction thereof, up to 25% when a return is not made and filed (*Section 18681*) or when not filed after notice, demand and levy (*Section 18682*). If the sum of the penalties under Section 18681 and 18682, are less than Section 18684.2, only the penalty under Section 18684.2 shall apply. Previously, a taxpayer who filed a return at the time due, April 15, but who did not pay his tax was liable for interest of 6% per year on the total amount owed (*Section 18686*) or 6% per year if he made an underpayment of estimated tax (*Section 18685.3*). A possible effect of this amendment is to discourage those taxpayers who file returns without payment, thereby paying the state an interest rate of 6 percent per year (*Section 18686*) in lieu of borrowing money at a much greater interest rate to pay their taxes.

References:
1) 26 U.S.C. §6653(a) (1964).
2) FEDERAL TAX PROCEDURE, *Criminal & Civil Tax Fraud* §8.10 CONTINUING EDUCATION OF THE BAR (1968).
3) S. GUTKIN, TAX AVOIDANCE AND TAX EVASION 220 (1958).

Taxation; filing by mail

Revenue and Taxation Code §§166, 2512, 2512.5 (amended); 165 (repealed).

AB 1543; STATS 1970, Ch 748

The amendment to Section 166 (*relating to Property Taxation*) establishes a statute of limitations of one year from the deadline applicable to the original filing in which a taxpayer may file a statement of affidavit asserting the timely filing of the previously required statement, affidavit, application or any other paper or document required to be filed with a taxing agency of California. This provision shall not apply to any statement, affidavit, application, or any other paper or document asserting timely filing of a property statement or any statement made by a taxpayer in connection with an escape assessment imposed pursuant to Section 531.

This Section does not apply to the filing of payments (payment was deleted from the Section by this amendment) but only to any statement, affidavit, application or any other paper or document required to be filed with a taxing agency.

Section 2512 and 2512.5 (*concerning when postmark date or mere deposit of an envelope will be deemed to be made within the specified time prescribed for making payments*) are amended to provide that the taxing agency (*defined in Section 121*) need not accept a payment actually received in the mail though postmarked (*Section 2512*) or deposited (*Section 2512.5*) in accord with these Sections if it is received more than 30 days after the date and time set for payment.

This amendment substituted the phrase "actually received in the mail" for the word "received" to provide more specifically for this exception.

References:
1) 3 WITKIN, SUMMARY OF CALIFORNIA LAW, *Taxation* §71 (Supp. 1969).
2) CONTINUING EDUCATION OF THE BAR, REVIEW OF SELECTED 1968 CODE LEGISLATION 242.

Sales Tax Exemption

Revenue and Taxation Code §6396 (new).

AB 1081; STATS 1970, Ch 1457

(Effective September 19, 1970)

This Section adds gross receipts of certain personal property transactions already exempt from sales tax. Previously gross receipts from the sale of the following tangible personal property were exempt from state sales tax: (1) sales to the United States, its unincorporated agencies and instrumentalities, any incorporated agency or corporation wholly owned by the United States, and the American Red Cross, its chapters and branches (*Section 6381*), (2) sales to common carriers where the property is shipped by the seller via the purchasing carrier to a point of destination outside California (*Section 6385*), (3) sales to a holder of a valid seller's permit issued under Section 6068 when the property is used by the purchaser outside California in his performance of a contract to improve real property (*Section 6386*), and (4) sales to one engaged in exporting where the property is delivered to a forwarding agent, export packer, or other person engaged in the business of preparing goods for export (*Section 6387*).

The new Section 6396 exempts gross receipts of tangible personal property if such property, pursuant to the contract of sale, is required to be shipped and is shipped to a point outside California by the retailer through (1) facilities operated by the retailer, or (2) delivery by the retailer to a carrier, customs broker, or forwarding agent for shipment to an out-of-state destination.

For purposes of this Section a carrier is defined as a person or firm engaged in the business of transporting, for compensation, tangible personal property owned by other persons. A forwarding agent is defined as a person or firm engaged in the business of preparing property for shipment or arranging for its shipment.

Reference:
1) 3 WITKIN, SUMMARY OF CALIFORNIA LAW, *Taxation* §§138, 139 (7th ed. 1960); (Supp. 1969).

Property Taxation; homeowner exemption

Revenue and Taxation Code §255.1 (new).

AB 442; STATS 1970, Ch 203

(Effective June 15, 1970)

Chapter 203 allows a county assessor to grant a reasonable extension of time to a homeowner when the homeowner filed a claim for the homeowner's property tax exemption on time, but the filing was otherwise defective.

If in the assessor's judgment good cause exists, one such extension of up to six months from the original due date is allowed. The statute does not specify factors which would constitute good cause. If the assessor has not been able to find and notify the homeowner of the defect in time to give a reasonable time for resubmission, he may allow the homeowner up to three additional months to correct the defect. The homeowner's property tax exemption is that provided for in Section 218.

Reference:

1) 3 WITKIN, SUMMARY OF CALIFORNIA LAW, *Taxation* §72 (7th ed. 1960), (Supp. 1969); 3 WITKIN, SUMMARY OF CALIFORNIA LAW, *Taxation* §68 (Supp. 1969).

Involuntary Conversion of Property

Revenue and Taxation Code §24944 (amended).

AB 1801; STATS 1970, Ch 641

Chapter 641 extends the period of time under Section 24944 from one year to two years during which a taxpayer under the Bank and Corporation Tax Law may replace involuntarily converted property and have the gain from such replacement subject to limited recognition for tax purposes.

Prior to amendment, Section 24944 allowed the recipient of proceeds from an involuntary or compulsory conversion of property (as a result of destruction, theft, condemnation or threat or imminence thereof) to purchase within one year property similar or related in service to that property converted and thereby limit the taxable gain to that amount realized upon conversion which exceeds the cost of the other property purchased.

This amendment extends the period within which a purchase may be made to two years from the date the original property was converted, or the earliest date of the threat or imminence of conversion, whichever is earlier.

References:

1) 18 CAL. ADM. CODE 25035(a).

2) 26 U.S.C.A. (I.R.C. 1954) §1033 (a) (3).

Inheritance Tax Appraisers

Code of Civil Procedure §§580a, 726 (amended); Education Code §29007 (amended); Probate Code §§605 (new); 600, 606-609.5, 611, 644, 664-666, 784, 1174, 1550, 1901 (amended); 605 (repealed); Revenue and Taxation Code §§ 14771.5, 14772, 14773, 14774.5, 14778, 14778.5 (new); 13315, 13988, 14192, 14307, 14501-14507, 14511, 14512, 14514, 14515, 14531, 14534-14536, 14552-14555, 14574-14576, 14591, 14592, 14601, 14734, 14735, 14771, 15572-15577, 16503-16505 (amended); 14772-14774 (renumbered).

SB 361; STATS 1970, Ch 1282

Chapter 1282 enacts significant revisions to the selection and duties of state inheritance tax appraisers (*hereinafter titled tax referees pursuant to this act*).

Probate Code Section 600 provides that the executor or administrator, within three months after his appointment, must file with the clerk of the court an inventory and appraisement of the decedent's estate. By this amendment the inventory and appraisement now must be prepared in such form as to set down each item separately with the fair market value thereof at the time of the decedent's death in dollars and cents in figures opposite the respective items.

In addition, prior to this amendment, Section 600 provided that if the whole estate consists of money in the hands of the executor or administrator, no appraisement was required, but an inventory was still required. This provision has been deleted.

Probate Code Section 605 has been repealed and a new Section 605 has been added. This Section establishes that the appraisement shall be made by the executor or administrator and an inheritance tax referee as follows: (1) Appraise at fair market value moneys, currency, cash items, bank accounts, and amounts on deposit with any financial institution, and the proceeds of life and accident insurance policies and retirement plans payable upon death in lump sum amounts, excepting therefrom such items whose fair market value is, in the opinion of the executor or administrator, an amount different from the ostensible value or specified amount. (2) All assets other than above, shall be appraised by an inheritance tax referee appointed by the court or judge. In addition, the duties of the executor, administrator and referee to furnish information as required by the State Controller are set out. Also the executor or administrator or his attorney shall not be entitled to receive compensation for extraordinary services by reason of appraising any asset pursuant to this Section.

Probate Code Section 608 as amended, provides that the appraisement be subscribed by the appraiser under oath and under penalty of perjury. Previously, there was no provision for penalty of perjury. Also, previously there was the requirement that each item be set down separately with the value of the items. This requirement has been deleted.

Probate Code Section 609 changes the appraiser's commissions from each estate appraised by him. His fees are now as follows: for the first $5,000 or fraction thereof, $5.00; for the next $495,000, one-tenth of 1%; for all over $500,000 a fee of one-twentieth of 1% thereof. As before he is allowed his actual and necessary expenses.

Probate Code Section 611 now requires that when property not included in the inventory is discovered, it must be appraised and inventoried and both documents must be filed with the clerk of the court. Previously only the inventory had to be filed.

Probate Code Section 666 is amended to delete the provision which allowed that, in appraisal of homesteads and exempt property, any two of the appraisers concurring may discharge the duties imposed upon the three and make the report. Now one report is filed and the court either accepts or rejects it. Further, the report is made by one inheritance tax referee rather than 3 appraisers.

Probate Code Section 1174 now provides that in establishing the fact of death petitions, or affidavits in support thereof, may be received in evidence and acted upon by the court with the same force and effect as if the petitioner or affiants were personally present to testify. The court may render judgment thereon establishing the fact of death. The judgment shall be prima facie evidence of the fact of death. The presumption established by this Section is a presumption affecting the burden of producing evidence. Previously, Section 1174 required that the court take evidence for or against the petition and then render judgment; the judgment being prima facia evidence of death.

Probate Code Section 1550 is amended to provide that when a guardian is appointed for a deceased ward, the guardian and an inheritance tax referee shall appraise the estate. The guardian may appraise the assets which an executor or administrator could appraise under Section 605 (*See analysis of Section 605 supra*).

Probate Code Section 1901 is amended to provide that when a conservator is appointed, the conservator and an inheritance tax referee shall appraise the estate in the same manner as provided under Section 605 for executors or administrators.

Section 14501 of the Revenue and Taxation Code is amended to provide that in ascertaining the clear market value of any property appraised by an executor or administrator (*see Probate Code Section 605, supra*), the inheritance tax referee may require the executor or administrator to furnish information as will enable the referee to determine the accuracy of the appraisal made by the executor or administrator. Previously, there was no requirement that this information be furnished. The Section is further amended to permit the Judicial Council to provide rules for the method of distribution within each county of appointments of cases to inheritance tax referees from the panel.

Revenue and Taxation Code Section 14771 is amended to require that inheritance tax referees be appointed by the State Controller from among persons passing a State administered qualification examination. At least one referee must be appointed in each county. Such appointments shall be made on the basis of merit without regard to sex, race, religion, national origin, marital status or political affiliation. In addition this Section provides that the Controller shall stagger the terms of the first appointed referees so that one-quarter of the appointments expire in each of the first four years. Thereafter, the term will be four years. Once appointed, a referee remains eligible for reappointment. These changes are significant, as previously the Controller appointed inheritance tax referees to serve at his pleasure, without regard to qualifications.

Section 14771.5 is added to the Revenue and Taxation Code to provide that the Controller determines the time and places of inheritance tax referee examinations.

Section 14772 is added to the Revenue and Taxation Code to provide that the Controller may establish and amend standards of training, performance and ethics of inheritance tax referees. Such standards are public records.

Section 14773 is added to the Revenue and Taxation Code to establish procedures for removal of an inheritance tax referee for noncompliance with any standard of training, performance or ethics. Further, the Controller may also remove, at his pleasure, at least one inheritance tax referee, but not more than 10 percent of the referees in any one county.

Section 14774.5 is added to the Revenue and Taxation Code to provide that whenever property is required to be appraised for the purpose of determination of tax under this part, the appraisal shall be made in the manner provided by Probate Code Section 605 (*see supra*).

The appraisal of all assets which an executor or administrator could make under Probate Code Section 605 may be made by the executor or administrator, and if there is none, by the petitioner in the court proceedings, and if there is neither executor, administrator or petitioner, then by the heir or transferee requesting consent to transfer or other action of the Controller or inheritance tax referee.

Section 14778 is added to the Revenue and Taxation Code to provide that no inheritance tax referee, or candidate therefor, shall be involved in soliciting, receiving or contributing any assessment, subscription, contribution, or political service for any campaign for the office of Controller. If the office is other than Controller, the limit is $200.00 to any party or candidate in any one year. Any violation is a misdemeanor.

Section 14778.5 provides that the Controller cannot appoint anyone who violates Section 14778, and any such appointment is void; however, acts performed by such person prior to removal are valid.

Revenue and Taxation Code Section 14771.5 (*Controller sets qualifications for and places and times of examination*) shall become operative November 23, 1970, and the remainder of the act shall become operative July 1, 1971 as to all decedents except those with respect to whom a probate or other proceeding instituted prior to said time is pending in which inheritance tax due by reason of the decedent's death may be fixed.

Any Section in this Chapter not specifically mentioned herein has only been amended technically to conform with the above discussed changes, usually for the purpose of changing the term inheritance tax appraiser to inheritance tax referee.

Inheritance Tax; powers of appointment

Revenue and Taxation Code §13694 (amended).
SB 513; STATS 1970, Ch 514

This amendment to Section 13694 revises the provisions for taxing powers of appointment. Powers of appointment are classified as general or limited. For inheritance tax purposes, a general power is one which the donee of the power may exercise in favor of himself, his estate, his creditors or the creditors of his estate (*Revenue and Taxation*

Code §13692). Powers which may not be so exercised are limited powers.

Under present law, all transfers made subject to a power of appointment, whether general or limited, are taxed in the estate of the donor as though the property subject to the power passed from the decedent to the donee rather than to the beneficiaries who actually received it upon the donee's exercise of the power.

This amendment to Section 13694 is aimed at the type of trust commonly referred to as a "sprinkling" or "spraying" trust. A "sprinkling" trust is a transfer when the trustee is granted a power limited to making discretionary payments of the principle or income for the benefit of trust beneficiaries. Under this change, a "sprinkling" trust in which the donee may not be a beneficiary of the trust will be treated as a transfer to the beneficiaries rather than a power of appointment. Thus property subject to this type of transfer would be taxed to the *ultimate beneficiaries rather than the donee.*

References:
1) 3 WITKIN, SUMMARY OF CALIFORNIA LAW, *Taxation* §115 (7th ed. 1960), (Supp. 1969).
2) Barnett, *California Inheritance and Gift Taxes A Summary*, 43 CAL. L. REV. 55 (1955); Comment, *Inheritance and Transfer Taxes: Jurisdiction to Tax Exercise of Power of Appointment by Resident Donee*, 39 CAL. L. REV. 150 (1951).

Taxation; disposition of property

Revenue and Taxation Code §§17233, 17235, 18219, 18220, 24422.5, 24662 (new); 17571, 18081, 18182, 18211, 24941 (amended); 17292 (repealed).

AB 1881; STATS 1970, Ch 1276

This Chapter was passed as a federal tax conformity measure primarily to tighten up the "hobby loss" provisions of state tax law.

Section 17233 is added to provide that in the case where an individual is engaged in some activity (*i.e., some form of business enterprise as raising farm livestock*) but such activity is not engaged in for profit, for tax purposes it will be treated as a "hobby" and deductions attributable to such activity may only be deducted from the "hobby" income. However, subsection (d) provides an exception to this provision when, during a period of five consecutive years of engaging in a specific activity, if during two of the five years, gross income derived from the activity exceeded the deductions for those years, a presumption arises that the activity is engaged in for profit. If the activity involves race horses for breeding, training or showing, the profit need only occur in two years out of seven consecutive years. If it can be established that the activities are for profit, hobby losses may be deducted from other income. The State Franchise Tax Board has the burden of overcoming this presumption once it arises.

Section 17235 (*applicable to individual taxpayers*) and Section 24422.5 (*applicable to corporate taxpayers*) are added to provide that costs incurred for planting, cultivation and maintenance of citrus groves incurred before the end of the fourth taxable year after the trees are planted must be capitalized. However, subdivision (b) of both Sections provides that where costs are incurred for replanting because of damage and destruction caused by freezing, disease, drought, pests, or casualty, such costs may be deducted from other income. Also, if the trees were planted or replanted prior to enactment of this Chapter, these Sections will not apply to limit deductions for the cost of planting, cultivating and maintenance. Prior to enactment of these Sections, taxpayers were permitted to deduct from total income, current expenditures for citrus grove development.

Section 17571 (*applicable to individual taxpayers*) and Section 24662 (*applicable to corporate taxpayers*) are amended to permit taxpayers who report by the cash receipts and disbursements method of accounting to defer reporting any insurance payments received as a result of crop destruction or damage until the tax year following the damage if they can establish that the income from the damaged crops would have been reported in a subsequent taxable year. Previously, the taxpayer had to report crop damage insurance payments in the year they were received along with income from crops of a prior year causing a double taxation for that year.

Section 18081 (*applicable to individual taxpayers*) and Section 24941 (*applicable to corporate taxpayers*) are both amended to provide that livestock of different sexes are not property of like kind for the purposes of tax-free exchange of male calves for female calves.

Section 18182 is amended to extend the time limit the taxpayer must hold cattle and horses in order to be eligible for capital gains treatment. Previously, he had to hold such animals for twelve months. The requirement is now extended to 24 months.

Section 18211 is amended to eliminate the special exemption for livestock from the general personal property depreciation recapture rules. Consequently, the gain on the sale of purchased livestock to which depreciation deductions have been claimed will be taxed as ordinary income rather than capital gain to the extent of the depreciation taken.

Section 18219 is added to provide revisions to the previous method used by individual taxpayers for deducting farm land expenditures. Previously, a taxpayer could deduct expenditures for soil and water conservation and land clearing during the current taxable year. Under the new Section, applicable to farm lands held for less than ten years, disposed of after December 31, 1969, such expenses must be recaptured as ordinary income on the sale of the property according to a graduated scale included in the Section. An exception to Section 18219 is where such expenses are recaptured under the farm loss recapture provisions as provided in new Section 18220. Such expenditures may not be accounted for under Section 18219. The State Franchise Tax Board is authorized to prescribe rules and regulations governing certain exceptions to Section 18219.

Section 18220 is added to provide stricter rules regarding deductions for farm losses and expenditures for developing business assets. Under the new requirements excess farm loss deductions from non-farm income is recaptured when certain farm assets are sold. Farm losses include losses from farming or horse racing. The provisions of this Section would not apply to accrual-basis farmers who employ inventories and who capitalize all expenditures. Also this Section would not apply to farmers whose gross income is less than $50,000 or whose net loss is less than $25,000 during the taxable year. Those farmers who come within the provisions of the Section (*those not subject to the above exceptions*) may continue to deduct farm losses from non-farm income but must keep a record of such deductions in excess of $25,000 in a special account known as the excess deductions account. Each year they are required to add any losses over $25,000 to this account or subtract from the account a sum equal to the net profit from farm activity. When any of the following types of farm property are sold: (a) depreciable personal property held for more than six months; (b) cattle or horses held for two years or more; (c) land held for more than six months; or (d) unharvested crops growing on land held for more than six months; the capital gain from such sales is compared with the balance in the excess deductions account. That amount of income from the gain equal to the income in the excess deductions account will be taxed as ordinary income and the balance will be taxed as a capital gain. This also reduces the balance in the excess deductions account by the amount used to offset any capital gain.