

Instructions for Schedule CA (540)

References to these instructions are to the Internal Revenue Code (IRC) as of **January 1, 2005**, and the California Revenue and Taxation Code (R&TC).

What's New

Registered Domestic Partners (RDP)

Effective for taxable years beginning on or after January 1, 2007, RDPs under California law **must file** their California income tax returns using either the married/RDP filing jointly or married/RDP filing separately filing status. RDPs will have the same legal benefits, protections, and responsibilities as married couples unless otherwise specified.

If you entered into a same sex legal union in another state, other than a marriage, and that union has been determined to be substantially equivalent to a California registered domestic partnership, effective for taxable years beginning on or after January 1, 2007, you are required to file a California income tax return using either the married/RDP filing jointly or married/RDP filing separately filing status. For more information on what states have legal unions that are considered substantially equivalent, go to our Website at www.ftb.ca.gov and search for **RDP**.

For purposes of California income tax, references to a spouse, a husband, or a wife also refer to a California Registered Domestic Partner (RDP), unless otherwise specified. When we use the initials (RDP) they refer to both a California Registered Domestic "Partner" and a California Registered Domestic "Partnership," as applicable. For more information on RDPs, get FTB Pub. 737, Tax Information for Registered Domestic Partners.

Conformity

For updates regarding the following federal act, go to our Website at www.ftb.ca.gov and search for **conformity**.

- Small Business and Work Opportunity Tax Act of 2007
- Mortgage Forgiveness Debt Relief Act of 2007

General Information

In general, California law conforms to the Internal Revenue Code (IRC) as of January 2005. However, there are continuing differences between California and federal law. When California conforms to federal tax law changes, we do not always adopt all of the changes made at the federal level. For more information, go to our Website at www.ftb.ca.gov and search for **conformity**. Additional information can be found in FTB Pub. 1001, Supplemental Guidelines to California Adjustments, and the Business Entity tax booklets.

The instructions provided with California tax forms are a summary of California tax law and are only intended to aid taxpayers in preparing their state income tax returns. We include information that is most useful to the greatest number of taxpayers in the limited space available. It is not possible to include all requirements of the California Revenue and Taxation Code (R&TC) in the tax booklets. Taxpayers should not consider the tax booklets as authoritative law.

Military Personnel – Servicemembers domiciled outside of California, and their spouses/RDPs, may exclude the servicemember's military compensation from gross income when computing the tax rate on nonmilitary income. Requirements for military servicemembers domiciled in California remain unchanged. Military servicemembers domiciled in California must include their military pay in total income. In addition, they must include their military pay in California source income when stationed in California. However, military pay is not California source income when a servicemember is permanently stationed outside of California. For more information, get FTB Pub. 1032, Tax Information for Military Personnel.

Purpose

Use this schedule to make adjustments to your federal adjusted gross income and to your federal itemized deductions using California law.

Part I – Specific Line Instructions

Column A — Federal Amounts

Line 7 through Line 21

Enter on line 7 through line 21 the same amounts you entered on your federal Form 1040, line 7 through line 21; Form 1040A, line 7 through line 14b; or Form 1040EZ line 1, line 2, and line 3.

Registered Domestic Partners – RDPs will compute their limitations based on the combined federal adjusted gross income (AGI) of each partner's individual tax return filed with the Internal Revenue Service (IRS). For column A, line 7 through line 21, combine your federal amounts from each partner's individual federal tax return. For more information on RDPs, get FTB Pub. 737, Tax Information for Registered Domestic Partners.

The combined federal AGI used to compute limitations is different from the recalculated federal AGI used on Form 540, line 13. In situations where RDPs have no filing status adjustment, these amounts may be the same.

Line 22 – Total

Combine the amounts on line 7 through line 21.

Line 23 through Line 30 and Line 32 through Line 35

Enter the same amounts entered on your federal Form 1040, line 23 through line 30 and line 32 through line 35 or Form 1040A, line 16 through line 19.

Line 31a and Line 31b

Enter on line 31a the same amount entered on your federal Form 1040, line 31a. Enter on line 31b the social security number (SSN) or individual taxpayer identification number (ITIN) and last name of the person to whom you paid alimony.

Line 36

Add line 23 through line 31a and line 32 through line 35. However, if you made any of the adjustments described in the instructions for federal Form 1040, line 36 or if you claimed the foreign housing deduction from federal Form 2555, Foreign Earned Income, or Form 2555-EZ, Foreign Earned Income Exclusion, enter the amount from Form 1040, line 36 on this line.

Line 37 – Total

Subtract line 36 from line 22.

Column B and Column C — Subtractions and Additions

Use these columns to enter subtractions and additions to the federal amounts in column A that are necessary because of differences between California and federal law. Enter all amounts as positive numbers unless instructed otherwise.

You may need one or more of the following FTB publications to complete column B and column C:

- 1001, Supplemental Guidelines to California Adjustments
- 1005, Pension and Annuity Guidelines
- 1031, Guidelines for Determining Resident Status
- 1032, Tax Information for Military Personnel
- 1100, Taxation of Nonresidents and Individuals Who Change Residency

To get a publication or form go to our Website at www.ftb.ca.gov or see page 67 of your 540/540A tax booklet.

Line 7 – Wages, Salaries, Tips, etc.

Generally, you will not make any adjustments on this line. If you did not receive any of the following types of income, make no entry on this line in either column B or column C.

Active duty military pay. Special rules apply to active duty military taxpayers. Get FTB Pub. 1032, Tax Information for Military Personnel, for more information.

Sick pay received under the Federal Insurance Contributions Act and Railroad Retirement Act. California excludes this item from income.

Enter in column B the amount of these benefits included in the amount in column A.

Ridesharing fringe benefit differences. Under federal law, qualified transportation benefits are excluded from gross income. Under the Revenue and Taxation Code, there are no monthly limits for the exclusion of these benefits and California's definitions are more expansive. Enter the amount of ridesharing benefits received and included in federal income on line 7, column B.

Exclusion for compensation from exercising a California Qualified Stock Option (CQSO). To claim this exclusion:

- Your earned income is \$40,000 or less from the corporation granting the CQSO.
- The market value of the options granted to you must be \$100,000 or less.
- The total number of shares must be 1,000 or less.
- The corporation issuing the stock must designate that the stock issued is a California qualified stock option at the time the option is granted.

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

Exclusion for Medical Expenses Reimbursement. California allows an exclusion from gross income for employer-provided accident, health insurance, and medical expense reimbursement for registered domestic partners and the partner's dependents if they were not previously deducted. Self-employed individuals may also claim a deduction for health insurance costs paid for themselves, their spouse or registered domestic partner, and their dependent(s), including the dependent(s) of their RDP. Enter the amount included in federal income in column B.

Compensation of merchant seamen, military servicemembers, rail, motor, and aircraft carriers. Exclude the following from gross income: compensation for the performance of duties of certain merchant seamen, rail carriers, motor carriers, aircraft carriers, and military servicemembers.

Line 8 – Taxable Interest Income

If you did not receive any of the kinds of income listed below, make no entry on this line in either column B or column C.

Enter in column B the interest you received from:

- U.S. savings bonds (except for interest from series EE U.S. savings bonds issued after 1989 that qualified for the Education Savings Bond Program exclusion).
- U.S. Treasury bills, notes, and bonds.
- Any other bonds or obligations of the United States and its territories.
- Interest from Ottoman Turkish Empire Settlement Payments.
- Interest income from children between the ages of 14 and 18. (For more information, get FTB Pub. 1001, Supplemental Guidelines to California Adjustments.)
- Interest income from children under the age of 14, included on the parent's or child's federal return and reported on the California return by the opposite taxpayer.

Certain mutual funds pay "exempt-interest dividends." If the mutual fund has at least 50% of its assets invested in tax-exempt U.S. obligations and/or in California or its municipal obligations, that amount of dividend is exempt from California tax. The proportion of dividends that are tax-exempt will be shown on your annual statement or statement issued with Form 1099-INT.

Enter in column C the interest you identified as tax-exempt interest on your federal Form 1040 (or Form 1040A), line 8b, **and** which you received from:

- The federally exempt interest dividends from other states, or their municipal obligations and/or from mutual funds that do not meet the 50% rule above.
- Non-California state bonds.
- Non-California municipal bonds issued by a county, city, town, or other local government unit.
- Obligations of the District of Columbia issued after 12/27/73.

- Non-California bonds if the interest was passed through to you from S corporations, trusts, partnerships, or Limited Liability Companies (LLCs).
- Interest or other earnings earned from a Health Savings Account (HSA) are not treated as taxed deferred. Interest or earnings in a HSA are taxable in the year earned.
- Interest on any bond or other obligation issued by the Government of American Samoa.
- Interest income from children under the age of 14, excluded on the parent's or child's federal return and reported on the California return.

Make no entries in either column B or column C for interest you earned on Federal National Mortgage Association (Fannie Mae) Bonds, Government National Mortgage Association (Ginnie Mae) Bonds, and Federal Home Loan Mortgage Corporations (FHLMC) securities, or grants paid to low income individuals.

Get FTB Pub. 1001, Supplemental Guidelines to California Adjustments, if you received interest income from the following sources:

- Loans made in an enterprise zone (EZ) or the former Los Angeles Revitalization Zone (LARZ).
- Items listed above passed through to you from S corporations, trusts, estates, partnerships, or LLCs.

Line 9 – Ordinary dividends

Generally, no difference exists between the amount of dividends reported in Column A and the amount reported using California law. However, California taxes dividends derived from other states and their municipal obligations.

Add dividends received from the following and enter in column B:

- Non-cash patronage dividends from farmers' cooperatives or mutual associations.
- Dividend income for children between the ages of 14 and 18. (For more information, get FTB Pub. 1001, Supplemental Guidelines to California Adjustments.)
- Dividend income from children under the age of 14, included on the parent's or child's federal return and reported on the California return by the opposite taxpayer.

Add dividends received from the following and enter in column C:

- Controlled foreign corporation dividends in the year distributed.
- Regulated investment company (RIC) capital gains in the year distributed.
- Distributions of pre-1987 earnings from an S corporation.
- Non-cash patronage dividends from farmers' cooperatives or mutual associations.
- Dividend income from children under the age of 14, excluded on the parent's or child's federal return and reported on the California return.

Get FTB Pub. 1001, Supplemental Guidelines to California Adjustments, if you received dividends from:

- Non-cash patronage dividends from farmers' cooperatives or mutual associations.
- A controlled foreign corporation.
- Distributions of pre-1987 earnings from S corporations.
- Undistributed capital gains for regulated investment company (RIC) shareholders.

Line 10 – Taxable refunds, credits, or offsets of state and local income taxes

California does not tax the state income tax refund received in 2007. Enter in column B the amount of state tax refund entered in column A.

Line 11 – Alimony Received

If you are a nonresident alien and received alimony not included in your federal income, enter the alimony on this line in column C. Otherwise, make no entry on this line.

Line 12 – Business Income or (Loss)

Adjustments to federal business income or loss you reported in column A generally are necessary because of the difference between California and federal law relating to depreciation methods, special credits, and

accelerated write-offs. As a result, the recovery period or basis used to figure California depreciation may be different from the amount used for federal purposes.

Adjustments are figured on form FTB 3885A, Depreciation and Amortization Adjustments, and are most commonly necessary because of the following:

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

Use form FTB 3801, Passive Activity Loss Limitations, to figure the total adjustment for line 12 if you have:

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

Use form FTB 3885A to figure the total adjustment for line 12 if you have:

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

Get FTB Pub. 1001, Supplemental Guidelines to California Adjustments, for more information about:

Income related to:

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

Basis adjustments related to:

- Property acquired prior to becoming a California resident.
- Sales or use tax credit for property used in an EZ, Local Agency Military Base Recovery Area (LAMBRA), Targeted Tax Area (TTA), or former LARZ.
- Reduced recovery periods for fruit-bearing grapevines replaced in a California vineyard on or after 1/1/92 as a result of phylloxera infestation; or on or after 1/1/97 as a result of Pierce's disease.
- Expenditures for tertiary injectants.
- Property placed in service on an Indian reservation after 1/1/94 and before 1/1/05.
- Amortization of pollution control facilities.
- Discharge of real property business indebtedness.
- Employer-paid child care program.
- Employer-paid child care plan.
- Vehicles used in an employer-sponsored ridesharing program.
- An enhanced oil recovery system.
- Joint Strike Fighter property costs.
- The cost of making a business accessible to disabled individuals.
- Property for which you received an energy conservation subsidy from a public utility on or after 1/1/95 and before 1/1/97.
- Research and experimental expenditures.

Business expense deductions related to:

- Wages paid in an EZ, LAMBRA, Manufacturing Enhancement Area (MEA), or TTA.
- Certain employer costs for employees who are also enrolled members of Indian tribes.
- Abandonment or tax recoupment fees for open-space easements and timberland preserves.
- Business located in an EZ, LAMBRA, or TTA.
- Research expense.
- Employer wage expense for the Work Opportunity Credit and Welfare-to-Work Credit.
- Pro-rata share of deductions received from a controlled foreign corporation by a U.S. shareholder.

- Interest paid on indebtedness in connection with company-owned life insurance policies.
- Premiums paid on life insurance policies, annuities, or endowment contracts issued after 6/8/97 where the owner of the business is directly or indirectly a policy beneficiary.
- Commercial Revitalization Deductions for Renewal Communities.

Line 13 – Capital Gain or (Loss)

Generally, no adjustments are made on this line. California taxes long and short term capital gains as regular income. No special rate for long term capital gains exists. However, the California basis of the assets listed below may be different from the federal basis due to differences between California and federal laws. If there are differences, use Schedule D (540), California Capital Gain or Loss Adjustment, to calculate the amount to enter on line 13.

- Gain on the sale of qualified small business stock which qualifies for the gain exclusion under IRC Section 1202.
- Basis amounts resulting from differences between California and federal law in prior years.
- Gain or loss on stock and bond transactions.
- Installment sale gain reported on form FTB 3805E, Installment Sale Income.
- Gain on the sale of personal residence where depreciation was allowable.
- Flow-through gain or loss from partnerships, fiduciaries, S corporations, or LLCs.
- Capital loss carryover from your 2006 California Schedule D (540).

Get FTB Pub. 1001, Supplemental Guidelines to California Adjustments, for more information about:

- Disposition of S corporation stock acquired before 1987.
- Gain on sale or disposition of qualified assisted housing development to low-income residents or to specified entities maintaining housing for low-income residents.
- Undistributed capital gain for RIC shareholders.
- Gain or loss on the sale of property inherited before 1/1/87.
- Capital loss carrybacks.
- Capital gain distribution for children between the ages of 14 and 18.

Line 14 – Other Gains or (Losses)

Generally, no adjustments are made on this line. However, the California basis of your other assets may differ from your federal basis due to differences between California and federal law. Therefore, you may have to adjust the amount of other gains or losses. Get Schedule D-1, Sales of Business Property.

Line 15 – Total IRA Distributions

Generally, no adjustments are made on this line. However, there may be significant differences in the taxable amount of a distribution (including a distribution from conversion of a traditional IRA to a Roth IRA), depending on when you made your contributions to the IRA. Differences also occur if your California IRA deductions were different from your federal deductions because of differences between California and federal self-employment income.

If the taxable amount using California law is:

- Less than the amount taxable under federal law, enter the difference in column B.
- More than the amount taxable under federal law, enter the difference in column C.

Get FTB Pub. 1005, Pension and Annuity Guidelines, for more information and worksheets for figuring the adjustment to enter on line 15, if any.

If you have an IRA basis and were a nonresident in prior years, you may need to restate your California IRA basis. Get FTB Pub. 1100, Taxation of Nonresidents and Individuals Who Change Residency.

Coverdell ESA formerly known as Education (ED) IRA – If column A includes a taxable distribution from an ED IRA, you may owe additional tax on that amount. Get form FTB 3805P, Additional Taxes on Qualified

Plans (Including IRAs) and Other Tax-Favored Accounts. Report only the taxable amount of the distribution on line 21f.

Line 16 – Total Pensions and Annuities

Generally, no adjustments are made on this line. However, if you received Tier 2 railroad retirement benefits or partially taxable distributions from a pension plan, you may need to make the following adjustments.

If you received a federal Form RRB 1099-R for railroad retirement benefits and included all or part of these benefits in taxable income in column A, enter the taxable benefit amount in column B.

If you began receiving a retirement annuity between 7/1/86 and 1/1/87 and elected to use the three-year rule for California purposes and the annuity rules for federal purposes, enter in column C the amount of the annuity payments you excluded for federal purposes.

You may have to pay an additional tax if you received a taxable distribution from a qualified retirement plan before reaching age 59½ and the distribution was not rolled over into another qualified plan. See Form 540, line 33 instructions; or form FTB 3805P, Additional Taxes on Qualified Plans (Including IRAs) and Other Tax-Favored Accounts.

Line 17 – Rental Real Estate, Royalties, Partnerships, S Corporations, Estates, Trusts, etc.

Adjustments to federal income or loss you reported in column A generally are necessary because of the difference between California and federal law relating to depreciation methods, special credits, and accelerated write-offs. As a result, the recovery period or basis used to figure California depreciation may be different from the recovery period or amount used for federal. For more information, see the instructions for column B and column C, line 12.

California law does not conform to federal law for material participation in rental real estate activities. Beginning in 1994, and for federal purposes only, rental real estate activities conducted by persons in real property business are not automatically treated as passive activities. Get form FTB 3801, Passive Activity Loss Limitations, for more information.

Use form FTB 3801, Passive Activity Loss Limitations, to figure the total adjustment for line 17 if you have:

- One or more passive activities that produce a loss.
- One or more passive activities that produce a loss **and** any nonpassive activity reported on federal Schedule E.

Use form FTB 3885A, Depreciation and Amortization Adjustments, to figure the total adjustment for line 17 if you have:

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

LLCs that are classified as partnerships for California purposes and limited liability partnerships (LLPs) are subject to the same rules as other partnerships. LLCs report distributive items to members on Schedule K-1 (568), Member's Share of Income, Deductions, Credits, etc. LLPs report to partners on Schedule K-1 (565), Partner's Share of Income, Deductions, Credits, etc.

Get FTB Pub. 1001, Supplemental Guidelines to California Adjustments, for more information about accumulation distributions to beneficiaries for which the trust was not required to pay California tax because the beneficiary's interest was contingent.

Line 18 – Farm Income or (Loss)

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

Use form FTB 3801, Passive Activity Loss Limitations, to figure the total adjustment for line 18 if you have:

- One or more passive activities that produce a loss.

- One or more passive activities that produce a loss **and** any nonpassive activity reported on federal Schedule F.

Use form FTB 3885A, Depreciation and Amortization Adjustments, to figure the total adjustment for line 18 if you have:

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

Line 19 – Unemployment Compensation

California excludes unemployment compensation from taxable income. Enter on line 19, column B the amount of unemployment compensation shown in column A.

Paid Family Leave Insurance (PFL) benefits, also known as Family Temporary Disability Insurance. Payments received from the PFL Program in 2007, are reported on your Form 1099-G in Column B, line 19. For additional information, get FTB Pub. 1001, Supplemental Guidelines to California Adjustments.

Line 20 – U.S. Social Security Benefits

California excludes U.S. social security benefits or equivalent Tier 1 railroad retirement benefits from taxable income. Enter in column B the amount of U.S. social security benefits or equivalent Tier 1 railroad retirement benefits shown in column A.

Line 21 – Other Income

a. California Lottery Winnings. California excludes California lottery winnings from taxable income. Enter in column B the amount of California lottery winnings included in the federal amount on line 21 in column A.

Make no adjustment for lottery winnings from other states. They are taxable by California. California and federal laws allow gambling losses only to the extent of reported gambling income. If you reduced gambling income for California lottery income, you may need to reduce the losses included in the federal itemized deductions on line 38. Enter these losses on line 41 as a negative number.

b. Disaster Loss Carryover from form FTB 3805V, Part III, line 6. If you have a California disaster loss carryover from your 2006 form FTB 3805V, Net Operating Loss (NOL) Computation and NOL and Disaster Loss Limitations – Individuals, Estates, and Trusts, enter that amount as a positive number in column B.

c. Federal NOL from Form 1040, line 21. If the amount on line 21 in column A includes a federal NOL, enter the amount of the federal NOL as a positive number in column C. Get form FTB 3805V, Net Operating Loss (NOL) Computation and NOL and Disaster Loss Limitations – Individuals, Estates, and Trusts, to figure the allowable California NOL.

d. NOL carryover from form FTB 3805V, Part III, line 5. The allowable NOL carryover under California law is different from the allowable NOL carryover under federal law. Use form FTB 3805V to figure the allowable California NOL and enter it as a positive number in column B.

e. NOL from form FTB 3805D, FTB 3805Z, FTB 3806, FTB 3807, or FTB 3809. Enter in column B the total NOL figured on the following forms.

- FTB 3805D, Net Operating Loss (NOL) Computation and Limitation – Pierce's Disease
- FTB 3805Z, Enterprise Zone Deduction and Credit Summary, line 5b
- FTB 3806, Los Angeles Revitalization Zone Deduction and Credit Summary, line 3b
- FTB 3807, Local Agency Military Base Recovery Area Deduction and Credit Summary, line 5b
- FTB 3809, Targeted Tax Area Deduction and Credit Summary, line 4b

f. Other (describe).

Reward from a crime hotline. Enter in column B the amount of a reward authorized by a government agency received from a crime hotline established by a government agency or nonprofit organization and that is included in the amount on line 21 in column A.

You may not make this adjustment if you are an employee of the hotline or someone who sponsors rewards for the hotline.

Federal foreign earned income or housing exclusion. Enter in column C the amount deducted from federal income on Form 1040, line 21.

Beverage container recycling income. Enter in column B the amount of recycling income included in the amount on line 21 in column A.

Rebates or vouchers from a local water agency, energy agency, or energy supplier. California law allows an income exclusion for rebates or vouchers from a local water agency, energy agency, or energy supplier for the purchase and installation of water conservation appliances and devices. Enter in column B the amount of this type of income included in the amount on line 21 in column A.

Original issue discount (OID) for debt instruments issued in 1985 and 1986. In the year of sale or other disposition, you must recognize the difference between the amount reported on your federal return and the amount reported for California purposes. **Issuers:** Enter the difference between the federal deductible amount and the California deductible amount on line 21f in column B. **Holders:** Enter the difference between the amount included in federal gross income and the amount included for California purposes on line 21f in column C.

Foreign income of nonresident aliens. Adjust federal income to reflect worldwide income computed under California law. Enter losses from foreign sources in column B. Enter foreign source income in column C.

Cost-share payments received by forest landowners. Enter in column B the cost-share payments received from the Department of Forestry and Fire Protection under the California Forest Improvement Act of 1978 or from the United States Department of Agriculture, Forest Service, under the Forest Stewardship Program and the Stewardship Incentives Program, pursuant to the Cooperative Forestry Assistance Act.

Foreign Income. If you excluded income exempted by U.S. tax treaties on your federal Form 1040 (unless specifically exempt for state purposes), enter the excluded amount in Column C. If you claimed foreign earned income or housing cost exclusion on your federal Form 1040 (under IRC Section 911), see the instructions for line 21.

Compensation for False Imprisonment. California excludes compensation for false imprisonment from income. Enter the amount of compensation on line 21f, column B.

Coverdell (ESA) Distributions. If you received a distribution from a Coverdell ESA, report only the taxable amount of the distribution on line 21f.

Grants paid to low-income individuals. California excludes grants paid to low-income individuals to construct or retrofit buildings to make them more energy efficient. Federal has no similar exclusion. Enter on line 21f, column B the amount of this type of income.

Health Savings Account (HSA) Distributions for unqualified medical expense. Distributions from a HSA not used for qualified medical expenses, and included in federal income, are not taxable for California purposes. Enter the distribution not used for qualified medical expenses on line 21f, column B.

California National Guard Surviving Spouse & Children Relief Act of 2004. Death benefits up to \$10,000 received from the State of California by a surviving spouse/RDP or member-designated beneficiary of certain military personnel killed in the performance of duty is excluded from gross income. Military personnel include the California National Guard, State Military Reserve, or the Naval Militia. If you reported a death benefit on line 21, column A, enter the death benefit amount in column B.

Ottoman Turkish Empire Settlement Payments. If you received settlement payments as a person persecuted by the regime that was in control of the Ottoman Turkish Empire from 1915 until 1923 your gross income does not include those excludable settlement payments, or interest, received by you, your heirs, or your estate for payments received on or after January 1, 2005. If you reported settlement payments on line 21, column A, enter the amount of settlement payments in column B.

Mortgage relief upon sale or other disposition of principal residence. For taxable years 2007 through 2009, federal law allows an exclusion

of income from discharge of indebtedness from the disposition of your principal residence. If you were personally liable for a mortgage and you were relieved of liability for the mortgage indebtedness by disposition of the property then you may have realized a gain. To the extent the amount discharged exceeded the fair market value at the time of disposition, the difference is income from discharge of indebtedness. See federal Publication 544, Sales and Other Disposition of Assets, for more information. If you excluded income from the discharge of indebtedness on your federal return enter the amount in column C.

Hokie Spirit Memorial Fund exclusion. Enter in column C the amount excluded from federal income. For more information, get FTB Pub. 1001.

Line 22 – Total

Add line 7 through line 21f in column B and column C. Enter the totals on line 22.

Line 23 through Line 31a and Line 32 through Line 35 – California law is the same as federal law with the exception of the following:

- Line 23 (Educator expense) – Enter the amount from column A, line 23 to column B, line 23.

- Line 24 (Certain business expenses of reservists, performing artists, and fee-basis government officials) – If claiming a depreciation deduction as an unreimbursed employee business expense on federal Form 2106, you may have an adjustment in column B or column C.

- Line 25 (Health Savings Account (HSA) Deduction) – Federal law allows a deduction for contributions to an HSA account. California does not conform to this provision. Transfer the amount from Column A, line 25, to column B, line 25.

- Line 29 (Self-Employed Health Insurance Deduction) – Most people do not have any entry in column B or column C.

Enter on line 29, column C, the amount paid for health insurance coverage (established under your business) for your registered domestic partner and their dependents. Your total California deduction cannot exceed the limitations explained in the federal instructions. Do not include health insurance costs for any month you were eligible to participate in any subsidized health plan maintained by you or your registered domestic partner's employer.

Enter on line 29, column B, the amount of health insurance cost included in column A, line 29, for any month you were eligible to participate in any subsidized health plan maintained by your registered domestic partner's employer.

- Line 31a (Alimony Paid) – Enter the SSN or ITIN and last name of the person to whom you paid alimony.

If you are a nonresident alien and did not deduct alimony on your federal return, enter the amount you paid in column C.

- Line 32 (IRA Deduction) – If you are an active duty military servicemember domiciled outside of California, you may have an adjustment. See line 36.

California does not conform to the federal increase to the indexing of AGI requirements for IRAs. The phase-out for California remains at:

- Single or Head of Household \$50,000 - \$60,000
- Married/RDP filing joint or qualifying Widow(er) \$80,000 - \$100,000
- Individual not active, spouse participant \$150,000 - \$160,000

Federal amounts have increased to:

- Single or Head of Household \$52,000 - \$62,000
- Married filing joint/qualifying Widow(er) \$83,000 - \$103,000
- Individual not active, spouse participant \$156,000 - \$166,000

Compute your federal IRA deduction following the federal instructions using the federal IRA worksheet. Compute your California IRA deduction using the federal IRA worksheet using California phase-out amounts instead of federal amounts. Enter as an adjustment in column B, the difference between the amount determined for the federal IRA deduction and the California IRA deduction.

- Line 33 (Student Loan Interest Deduction) – California conforms to federal law regarding student loan interest deduction except for a spouse/RDP of a non-California domiciled military taxpayer residing in a community property state. Use the Student Loan Interest Deduction

Worksheet below to compute the amount to enter on line 33. See FTB Pub. 1032, Tax Information for Military Personnel, for more information.

Student Loan Interest Deduction Worksheet

- 1 Enter the total amount from Schedule CA (540), line 33, column A. If the amount on line 1 is zero, STOP. Enter zero on Schedule CA (540), column B. You are not allowed a deduction for California1
- 2 Enter the total interest you paid in 2007 on qualified student loans but not more than \$2,500 here ..2
- 3 From Form 1040, add line 33 (student loan interest deduction) to line 37 (AGI). Enter the result here3
- 4 Enter the total military income included in federal adjusted gross income (see FTB Pub. 1032)4
- 5 Subtract line 4 from line 35
- 6 Enter the amount shown below for your filing status.
 - Single, head of household, or qualifying widow(er) – \$55,000
 - Married/RDP filing jointly – \$110,000.....6
- 7 Is the amount on line 5 more than the amount on line 6?
☐ No. Skip lines 7 and 8, enter -0- on line 9, and go to line 10.
☐ Yes. Subtract line 6 from line 57
- 8 Divide line 7 by \$15,000 (\$30,000 if married/RDP filing jointly). Enter the result as a decimal (rounded to at least three places). If the result is 1.000 or more, enter 1.000 ..8
- 9 Multiply line 2 by line 89
- 10 **Student loan interest deduction.** Subtract line 9 from line 210
- 11 **Student loan interest adjustment.** Enter the result here. If line 1 is less than line 10, enter the difference on Schedule CA (540), column C.11

- Line 34 (Tuition and fees deduction) – Enter the amount from column A, line 34, to column B, line 34.
- Line 35 (Domestic production activities deduction) – California does not conform to the federal law regarding the domestic production activities deduction. If you made an adjustment on your federal return for domestic production activities, enter that amount in column B.

Registered Domestic Partner – RDPs will compute their limitations based on the combined federal adjusted gross income (AGI) of each partner's individual tax return filed with the Internal Revenue Service (IRS). For column A, line 23 through line 35, combine your federal amounts from each partner's individual federal tax return. For more information on RDPs, get FTB Pub. 737, Tax Information for Registered Domestic Partners.

Line 36 – Add line 23 through line 31a and line 32 through line 35 in column B and column C.

If you claimed the foreign housing deduction, include that amount in the total you enter in column B, line 36. Enter the amount and "Form 2555" or "Form 2555-EZ" on the dotted line next to line 36.

If you are active duty military and not domiciled in California and your IRA deduction was limited because of a federal AGI limitation, recalculate your deduction excluding your active duty military pay. If the recalculated amount is larger than the amount on line 32, column A, enter the difference between the two amounts in Column C, line 36. Enter the amount and "MPA Adjustment" on the dotted line next to line 36.

Line 37 – Total

Subtract line 36 from line 22 in column B and column C.

Also, transfer the amount from:

- Line 37, column B to Form 540, Side 1, line 14

If column B is a negative number, transfer the amount as a positive number to line 16.

- Line 37, column C to Form 540, Side 1, line 16

If column C is a negative number, transfer the amount as a positive number to line 14.

When itemizing deductions, go to Part II.

Part II – Specific Line Instructions

Line 38 – Federal Itemized Deductions

Enter the total amount of itemized deductions from your federal Form 1040, Schedule A, lines 4, 9, 15, 19, 20, 27, and 28.

Important: If you did not itemize deductions on your federal tax return but will itemize deductions on your California tax return, first complete federal Schedule A. Then complete Schedule CA (540), Part II, line 38 through line 44.

Line 39 – State, Local, Foreign Income Taxes, and General Sales Tax

Add the following amounts from federal Schedule A (Form 1040) and enter on line 39:

- Line 5, state and local income tax (including limited partnership tax and income or franchise tax paid by corporations), and State Disability Insurance (SDI) or Voluntary Plan Disability Insurance (VPDI).
- Line 8, foreign income taxes.

If you are deducting either local general sales and use taxes or state and local income taxes as an itemized deduction on federal Schedule A, line 5, enter the amount on Schedule CA, line 39.

For taxable years beginning in 2004 and 2005, the American Jobs Creation Act of 2004 allows taxpayers to elect to claim either local general sales and use taxes or state and local income taxes as an itemized deduction. If you are deducting either of these on line 5 of federal Schedule A, enter the amount on line 39.

Line 41 – Other Adjustments

Adoption-Related Expenses – If you deducted adoption-related expenses on your federal Form 1040, Schedule A and are claiming the adoption cost credit for the same amounts on your Form 540, enter the amount of the adoption cost credit claimed as a negative number on line 41.

Mortgage Interest Credit – If you reduced your federal mortgage interest deduction by the amount of your mortgage interest credit (from federal Form 8396, Mortgage Interest Credit), increase your California itemized deductions by the same amount. Enter the amount of your federal mortgage interest credit as a positive number on line 41.

Nontaxable Income Expenses – If, on federal Schedule A, you claim expenses related to producing income taxed under federal law but not taxed by California, enter the amount as a negative number on line 41.

You may claim expenses related to producing income taxed by California law but not taxed under federal law by entering the amount as a positive number on line 41.

Employee Business Expense – If you completed federal Form 2106, Employee Business Expense or Form 2106-EZ, Unreimbursed Employee Business Expense, prepare a second set of forms reflecting your employee business expense using California amounts (i.e., following California law).

Generally, California law conforms with federal law and no adjustment is needed. However, differences occur when:

- Assets (requiring depreciation) were placed in service before 1/1/87. Figure the depreciation based on California law.
- Federal employees were on temporary duty status. California does not conform to the federal provision that expanded temporary duties to include prosecutive duties, in addition to investigative duties. Therefore, travel expenses paid or incurred in connection with temporary duty status (exceeding one year), involving the prosecution (or support of the prosecution) of a federal crime, should not be included in the California amount.

Compare line 10 on the federal form and the form completed using California amounts. If the federal amount is larger, enter the difference as a negative number on line 41 (bracket the number). If the California amount is larger, enter the difference as a positive number on line 41.

Investment Interest Expense – Your California deduction for investment interest expense may be different from your federal deduction. Use form FTB 3526, Investment Interest Expense Deduction, to figure the amount to enter on line 41.

Interest Expense Deduction – Your California interest expense deduction may be different from your federal deduction. A deduction is allowed for interest paid on any loan or financed indebtedness from a utility company to purchase energy efficient equipment and products for California residences. Enter as a positive number on line 41.

Gambling Losses – California lottery losses are not deductible for California. Enter the amount of California lottery losses shown on federal Schedule A as a negative number on line 41.

Federal Estate Tax – Federal estate tax paid on income in respect of a decedent is not deductible for California. Enter the amount of federal estate tax shown on federal Schedule A as a negative number on line 41.

Generation Skipping Transfer Tax – Tax paid on generation skipping transfers is not deductible under California law. Enter the amount of expenses shown on federal Schedule A as a negative number on line 41.

State Legislator's Travel Expenses – Under California law, deductible travel expenses for state legislators include only those incurred while away from their place of residence overnight. Figure the difference between the amount allowed using federal law and the amount allowed using California law. Enter the difference as a negative number on line 41.

Charitable Qualified Contributions – Your California deduction may be different from your federal deduction. California limits the amount of your deduction to 50% of your federal adjusted gross income.

Charitable Contribution Carryover Deduction – If deducting a prior year charitable contribution carryover, and the California carryover is larger than the federal carryover, enter the additional amount as a positive number on line 41.

Health Savings Account (HSA) Distributions – If you received a tax-free HSA distribution for qualified medical expenses, enter the qualified expenses paid that exceed 7.5% of federal AGI as an adjustment to itemized deductions. To determine the amount of the itemized deduction adjustment:

- Calculate the medical expense deduction for California.
- Calculate the medical expense deduction for federal.
- Subtract the federal amount from the California amount. Enter the amount on line 41, as a positive amount.

Carryover Deduction Appreciated Stock Contributed to a Private Foundation prior to 1/1/02 – If deducting a charitable contribution carryover of appreciated stock donated to a private operating foundation prior to 1/1/02, and the fair market value allowed for federal purposes is larger than the basis allowed for California purposes, enter the difference as a negative number on line 41.

Interest on loans from utility companies – Taxpayers are allowed a tax deduction for interest paid or incurred on a public utility company financed loan that is used to purchase and install energy efficient equipment or products, including zone-heating products for a qualified residence located in California. Federal law has no equivalent deduction. Enter the amount as a positive number on line 41.

Medical benefits paid on behalf of registered domestic partners – Taxpayer benefits are extended to include the taxpayer's registered domestic partner and their dependent(s) for medical expenses and health insurance benefits that occur on or after 1/1/02. Federal law does not include this provision. Enter the amount as a positive number on line 41.

Private Mortgage Insurance (PMI) – If you took the deduction on Form 1040, Schedule A, line 13, then subtract the same amount on line 41.

Claim of Right – If you had to repay an amount that you included in your income in an earlier year, because at the time you thought you had an unrestricted right to it, you may be able to deduct the amount repaid from your income for the year in which you repaid it. Or, if the amount you repaid is more than \$3,000, you may take a credit against your tax for the year in which you repaid it, whichever results in the least tax.

If the amount repaid was not taxed by California, then no deduction or credit is allowed.

If you claimed a credit for the repayment on your federal return and are deducting the repayment for California, enter the allowable deduction as a positive amount on Schedule CA (540NR), line 41. Deductions of \$3,000 or less are subject to the 2% federal AGI limit.

If you deducted the repayment on your federal return and are taking a credit for California, enter the amount of the federal deduction as a negative amount on Schedule CA(540NR), line 41. To help you determine whether to take a credit or deduction, see the Repayment section of federal Publication 525, Taxable and Nontaxable Income. Remember to use the California tax rate in your computations. If you choose to take the credit instead of the deduction for California, add the credit amount on line 44, the total payment line, of the Form 540. To the left of the total, write "IRC 1341" and the amount of the credit.

Line 43 – California Itemized Deductions

Is the amount on Form 540, line 13 more than the amount shown below for your filing status?

Single or married/RDP filing separately \$155,416
Head of household \$233,129
Married/RDP filing jointly or qualifying widow(er) \$310,837

NO Transfer the amount from line 42 to line 43. Do not complete the worksheet.

YES Complete the Itemized Deductions Worksheet.

Note:

- If married or an RDP and filing a separate return, you and your spouse/RDP must either both itemize your deductions or both take the standard deduction.
- Also, if someone else can claim you as a dependent, claim the greater of the standard deduction or your itemized deductions. See the instructions for "California Standard Deduction Worksheet for Dependents" on page 11 or page 12 of the 540/540A tax booklet to figure your standard deduction.

Itemized Deductions Worksheet

1. Amount from Schedule CA (540), line 42. 1 _____
2. Using California amounts, add the amounts on federal Form 1040, Schedule A, line 4, line 14, and line 20 plus any gambling losses included on line 28 2 _____
3. Subtract line 2 from line 1 3 _____
If zero, STOP. Enter the amount from line 1 on Schedule CA (540), line 43.
4. Multiply line 3 by 80% (.80) 4 _____
5. Amount from Form 540, line 13. 5 _____
6. Enter the amount shown above for your filing status . . 6 _____
7. Subtract line 6 from line 5 7 _____
Note: If zero or less, STOP. Enter the amount from line 1 on Schedule CA (540), line 43.
8. Multiply line 7 by 6% (.06) 8 _____
9. Compare line 4 and line 8. Enter the smaller amount here. 9 _____
10. Total itemized deductions. Subtract line 9 from line 1. Enter here and on Schedule CA (540), line 43 10 _____