

1998 California Adjustments — Residents**CA (540)****Important:** Attach this schedule directly behind Form 540, Side 2.

Name(s) as shown on return

Social security number

Part I Income Adjustment Schedule

	A	B	C
	Federal Amounts (taxable amounts from your federal return)	Subtractions See instructions.	Additions See instructions.
Section A — Income			
7 Wages, salaries, tips, etc. See instructions before making an entry in column B or C	7		
8 Taxable interest income	8		
9 Ordinary dividends	9		
10 State tax refund. Enter the same amount in column A and column B	10		
11 Alimony received	11		
12 Business income or (loss)	12		
13 Capital gain or (loss)	13		
14 Other gains or (losses)	14		
15 Total IRA distributions. See instructions. (a)	(b)		
16 Total pensions and annuities. See instructions. (a)	(b)		
17 Rental real estate, royalties, partnerships, S corporations, trusts, etc.	17		
18 Farm income or (loss)	18		
19 Unemployment compensation. Enter the same amount in column A and column B	19		
20 Social security benefits (a)	(b)		
21 Other income.			
a California lottery winnings			
b Disaster loss carryover from FTB 3805V			
c Federal NOL (Form 1040, line 21)			
d NOL carryover from FTB 3805V			
e NOL from FTB 3805Z, 3806 or 3807			
f Other (describe)	21		
22 Total. Combine line 7 through line 21 in column A. Add line 7 through line 21f in column B and column C. Go to Section B	22		

Section B — Adjustments to Income

23 IRA deduction	23		
24 Student loan interest deduction	24		
25 Medical savings account deduction	25		
26 Moving expenses	26		
27 One-half of self-employment tax	27		
28 Self-employed health insurance deduction	28		
29 Keogh and self-employed SEP and SIMPLE plans	29		
30 Penalty on early withdrawal of savings	30		
31a Alimony paid. (b) Recipient's: SSN _____ - _____ - _____ Last name _____	31a		
32 Add line 23 through line 31a in columns A, B, and C.	32		
33 Total. Subtract line 32 from line 22 in columns A, B, and C. See the instructions for how to transfer the total to Form 540	33		

Part II Adjustments To Federal Itemized Deductions

35 Federal itemized deductions. Add the amounts on federal Sch. A (Form 1040), lines 4, 9, 14, 18, 19, 26 and 27	35	
36 Enter total of federal Sch. A, line 5 (state and local income tax and State Disability Insurance) and line 8 (foreign taxes only)	36	
37 Subtract line 36 from line 35.	37	
38 Other adjustments including California lottery losses. See instructions. Specify _____	38	
39 Combine line 37 and line 38.	39	
40 Is the amount on Form 540, line 13 more than the amount shown below for your filing status?		
Single or married filing separate \$116,777		
Head of household \$175,166		
Married filing joint or qualifying widow(er) \$233,556		
NO. Transfer the amount on line 39 to line 40.		
YES. Complete the Itemized Deductions Worksheet in the instructions for Sch. CA (540), line 40.		
Is the amount you entered on line 40 more than your standard deduction below?		
Single or married filing separate \$2,642		
Married filing joint, head of household or qualifying widow(er) \$5,284		
YES. Transfer the amount on line 40 to Form 540, line 18.		
NO. Enter your standard deduction on Form 540, line 18.		

1998 Depreciation and Amortization Adjustments**3885A**

Name(s) as shown on return	Business or activity to which form FTB 3885A relates	Social security number
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Part I Identify the activity as passive or nonpassive. See instructions.

- 1 ☐ This form is being completed for a passive activity. ☐ This form is being completed for a nonpassive activity.

Part II Election to Expense Certain Tangible Property (IRC Section 179).

2 Enter the amount from line 11 of the worksheet in the instructions 2

Part III Depreciation.	(a) Description of property placed in service during 1998	(b) Date placed in service	(c) California basis for depreciation	(d) Method	(e) Life or rate	(f) 1998 California depreciation deduction
3						

- 4 Add the amounts on line 3, column (f) 4
- 5 California depreciation for assets placed in service prior to 1998. 5
- 6 Total California depreciation from this activity. Add the amounts on line 2, line 4 and line 5 6
- 7 Total federal depreciation from this activity. Enter depreciation from your federal Form 4562, line 21 7
- 8 a If line 6 is more than line 7, enter the difference here and see instructions. 8a
- b If line 6 is less than line 7, enter the difference here and see instructions 8b

Part IV Amortization.	(a) Description of costs amortizable during 1998	(b) Date placed in service	(c) California basis for amortization	(d) Code section	(e) Period or percentage	(f) 1998 California amortization deduction
9						

- 10 Total California amortization from this activity. Add the amounts on line 9, column (f) 10
- 11 California amortization of costs that began before 1998. 11
- 12 Total California amortization from this activity. Add the amounts on line 10 and line 11 12
- 13 Total federal amortization from this activity. Enter amortization from your federal Form 4562, line 42 13
- 14 a If line 12 is more than line 13, enter the difference here and see instructions 14a
- b If line 12 is less than line 13, enter the difference here and see instructions 14b

1998 California Capital Gain or Loss Adjustment**D**

(a) Description of property (identify S corporation stock) Example: 100 shares of "Z" (S stock)	(b) Sales price	(c) Cost or other basis	(d) Loss. If (c) is more than (b), subtract (b) from (c)	(e) Gain. If (b) is more than (c), subtract (c) from (b)
1a				
1b				
2 Net gain or (loss) shown on California Schedule(s) K-1 from partnerships, S corporations, fiduciaries and limited liability companies 2				
3 Capital gain distributions (federal Form 1099-DIV, box 2a minus box 2d) 3				
4 Total 1998 gains from all sources. Add column (e) amounts of line 1a, line 1b, line 2 and line 3. 4				
5 1998 loss. Add column (d) amounts of line 1 and line 2. 5				
6 California capital loss carryover from 1997, if any. See instructions 6				
7 Total 1998 loss. Add line 5 and line 6. 7				
8 Combine line 4 and line 7. If a loss, go to line 9. If a gain, go to line 10 8				
9 If line 8 is a loss, enter the smaller of: (a) the loss on line 8; or (b) \$3,000 (\$1,500 if married filing a separate return). See instructions. 9				
10 Enter the amount from federal Form 1040, line 13 10				
11 Enter the California gain from line 8 or loss from line 9 11				
12 a If line 10 is more than line 11, enter the difference here and on Sch. CA (540 or 540NR) line 13, col. B 12a				
b If line 10 is less than line 11, enter the difference here and on Sch. CA (540 or 540NR), line 13, col. C 12b				

Instructions for Schedule CA (540)

These instructions are based on the Internal Revenue Code (IRC) as of **January 1, 1998** and the California Revenue and Taxation Code (R&TC).

General Information

Differences Between California and Federal Law

California legislation enacted in 1998 conforms California tax law to the Internal Revenue Code (IRC) as of January 1, 1998. However, there are continuing differences between California and federal tax law. California has not conformed to the changes made to the IRC by the Internal Revenue Service (IRS) Restructuring and Reform Act of 1998 (Public Law 105-206) and the Tax and Trade Relief Extension Act of 1998 (Public Law 105-277).

California law is different from federal law in the following areas:

IRC Section 179 expense deduction. The California maximum deduction is \$16,000; the federal maximum deduction is \$18,500. In many cases, this difference also affects the California basis and depreciation deduction for qualifying assets. See form FTB 3885A, Depreciation and Amortization Adjustments.

IRC Section 197 property. Property qualifying as Section 197 property for federal purposes is also Section 197 property for California purposes. However, for qualifying property acquired before January 1, 1994, the California adjusted basis as of January 1, 1994, must be amortized over the remaining federal amortization period. See form FTB 3885A.

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

Excluded gain on the sale of qualified small business stock held for more than five years. Get FTB Pub. 1001, Supplemental Guidelines to California Adjustments.

Roth IRAs. See the instructions for Column B and Column C, line 15.

Self-employed health insurance deduction. The California deduction for health insurance costs of self-employed individuals is 40%; the federal deduction is 45%. See the instructions for Column B and Column C, line 28.

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 (or on your federal Form 1040A, line 7 through line 13b; or on your federal Form 1040EZ line 1, line 2 and line 3). Also enter the following if applicable:

- The total IRA distribution received on line 15(a);
- The total pension or annuity distribution received on line 16(a); and
- The total social security retirement benefit received on line 20(a).

Line 22 — Total

Combine the amounts on line 7 through line 21.

Line 23 through Line 30

Enter the same amounts you entered on your federal Form 1040, line 23 through line 30 (or your Form 1040A, line 15 and line 16).

Line 31a and Line 31b

Enter on line 31a the same amount you entered on your federal Form 1040, line 31a. Enter on line 31b the social security number and last name of the person to whom you paid alimony.

Line 32 — Add line 23 through line 31a. However, if you made any of the adjustments described in the instructions for federal Form 1040, line 32 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 32 on this line.

Line 33 — Total

Subtract line 32 from line 22.

Column B and Column C — Subtractions and Additions

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

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

- 1001, Supplemental Guidelines to California Adjustments;
- 1005, Pension and Annuity Guidelines;
- 1005A, California Treatment of Roth IRA;
- 1031, Guidelines for Determining Resident Status; or
- 1032, Tax Information for Military Personnel.

To order a publication or form, see the back cover of your 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 kinds of income listed below, 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 for more information.

Ride-sharing benefits or sick pay received under the Federal Insurance Contributions Act and Railroad Retirement Act. California excludes these items from income. Enter in column B the amount of these benefits included in the amount in column A.

Income exempted by U.S. tax treaties (unless specifically exempt for state purposes also). If you excluded this income from your federal return, enter the excluded amount in column C. If you claimed foreign earned income or housing cost exclusion under IRC Section 911, see the instructions for line 21. Get FTB Pub. 1001 for more information.

Exclusion for compensation from exercising a California Qualified Stock Option (CQSO). To be eligible for this exclusion: your earned income from the corporation granting the CQSO must be \$40,000 or less; the market value of the options granted to you must be \$100,000 or less; and the total number of shares must be 1,000 or less. If you included in federal income an amount qualifying for this exclusion, enter that amount in column B.

Employer-provided meals. If your employer provided meals to you and other employees at the job site for the employer's convenience, you **may** have to include the value of those meals as a taxable fringe benefit for California purposes. California law has not conformed to the recent federal provision that allows employees to exclude (and employers to deduct) the value of such meals solely because the meals were provided to more than 50% of the employees. Check with your employer if you think that this might apply to you. If it does, enter in column C the amount of these benefits that were excluded for federal tax purposes.

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. Otherwise, follow the instructions below.

Enter in column B the interest you received from:

- U.S. saving 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; or
- Any other bonds or obligations of the United States and its territories;

Get FTB Pub. 1001 if you received interest income from the following sources:

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

Do not make 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.

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:

- 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 December 27, 1973; and
- Non-California bonds if the interest was passed through to you from S corporations, trusts, partnerships or LLCs.

Line 9 — Ordinary dividends

Generally, you will not make an adjustment on this line. However, certain mutual funds are qualified to pay "exempt-interest dividends" if at least 50% of their assets consist of tax-exempt government obligations. The portion of the exempt-

interest dividend that is tax-exempt will be shown on your annual statement from the mutual fund. If the California exempt-interest dividend amount is more than the federal exempt-interest dividend amount, enter the difference in column B.

Get FTB Pub. 1001 if you received dividends from:

- Noncash patronage dividends from farmers' cooperatives or mutual associations;
- A federal S corporation that is a California C corporation;
- A controlled foreign corporation;
- Distributions of pre-1987 earnings from S corporations;
- Undistributed capital gains for regulated investment company (RIC) shareholders; or
- Distributed capital gain dividends.

Line 10 – State Tax Refund

California does not tax the state income tax refund you received in 1998. Enter in column B the amount of state tax refund you entered in column A.

Line 11 – Alimony Received

If you are a nonresident alien and received alimony that was 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 the basis you should 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 business income or loss. Adjustments are figured on form FTB 3885A 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, and you must 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 below. Also, California does not conform to certain federal provisions. See the items listed under "General Information."

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

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

Use form FTB 3885A, Depreciation and Amortization Adjustments, 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); or
- Passive activities that produce gains.

Get FTB Pub. 1001 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; or
- 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, LARZ, Local Agency Military Base Recovery Area (LAMBRA) or Targeted Tax Area (TTA);
- Reduced recovery periods for fruit-bearing grapevines replaced in a California vineyard on or after 1/1/92 as a result of phylloxera infestation;
- Reduced recovery periods for fruit-bearing grapevines replaced in a California vineyard on or after 1/1/97 as a result of Pierce's disease;
- Expenditures for tertiary injectants;
- Certain property placed in service on an Indian reservation after 1/1/94 and before 12/31/03;
- Amortization of pollution control facilities;
- Discharge of real property business indebtedness;
- Employer-paid child care center and services;
- Employer-paid child care plan;
- Vehicles used in an employer-sponsored ridesharing program;
- An enhanced oil recovery system;
- 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; or
- Research and experimental expenditures.

Business expense deductions related to:

- Wages paid in an EZ, LARZ, LAMBRA or 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;
- Club dues or payments made to a club that restricts membership or the use of its services or facilities on the basis of age, sex, race, religion, color, ancestry or national origin;
- Lobbying expenses denied under IRC Section 162;
- Business located in an EZ, LARZ, 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; or
- Meals provided to more than 50% (but less than 100%) of employees on the employment premises for the employer's convenience.

Line 13 – Capital Gain or (Loss)

Generally, you will not make any adjustments on this line if you do not have any of the items listed below. Use Schedule D, California Gain or Loss Adjustment, if you have differences from:

- 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; or
- Capital loss carryover from your 1997 California Schedule D.

Get FTB Pub. 1001 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 regulated investment company (RIC) shareholders;
- Gain or loss on the sale of property inherited before 1/1/87; or
- Capital loss carrybacks.

Line 14 – Other Gains or (Losses)

Generally, you will not make any adjustments on this line. However, the California basis of your other assets may be different from the 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, to figure the adjustment.

Line 15 – Total IRA Distributions

Generally, you will not make any adjustments 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 may also occur if you changed your residency status after you first began making contributions to your IRA or 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; or
- More than the amount taxable under federal law, enter the difference in column C.

Traditional IRA – Get FTB Pub. 1005 for more information and worksheets for figuring the adjustment to enter on this line, if any.

Roth IRA – Get FTB Pub. 1005A, California Treatment of Roth IRA, for information about figuring the taxable gain and the California adjustment if you converted a traditional IRA to a Roth IRA.

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 Attributable to IRAs, Other Qualified Retirement Plans, Annuities, Modified Endowment Contracts and MSAs.

Line 16 – Total Pensions and Annuities

Generally, you will not make any adjustments 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 adjustments described below.

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.

Line 17 – Rental Real Estate, Royalties, Partnerships, S Corporations and 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 the basis you should use to figure California depreciation may be different from the recovery period or amount used for federal purposes, and you may need to make an adjustment to your income or loss. For more information about the types of income and deductions that often require adjustments, see the instructions for Column B and Column C, line 12.

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

- One or more passive activities that produce a loss; or
- 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); or
- Passive activities that produce gains.

Note: 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 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 the basis you should 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 Limitation (PALS), to figure the total adjustment for line 18 if you have:

- One or more passive activities that produce a loss; or
- 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); or
- Passive activities that produce gains.

Line 19 – Unemployment Compensation

Enter on line 19, column B the amount of unemployment compensation shown in column A.

Line 20 – Social Security Benefits

Enter in column B the amount of social security benefits or equivalent tier 1 railroad retirement benefits shown in column A.

Line 21 – Other Income

a. California Lottery Winnings. Enter in column B the amount of California lottery winnings included in the federal amount on line 21 in column A. **Note:** Do not include lottery winnings from other states. They are taxable to California.

b. Disaster Loss Carryover from FTB 3805V. If you have a California disaster loss carryover from your 1997 form FTB 3805V, Net Operating Loss (NOL) Computation and NOL and Disaster Loss Limitations, enter that amount as a positive number in column B.

c. Federal NOL deduction 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 deduction as a positive number in column C. Get form FTB 3805V to figure the allowable California NOL deduction.

d. NOL Carryover from FTB 3805V. 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 deduction, and enter it as a positive number in column B.

Note: If your 1997 form FTB 3805V has both disaster loss carryovers and NOL carryovers, you will need to separately state these two amounts. See line 21b for disaster loss carryovers.

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

- FTB 3805Z, Enterprise Zone Deduction and Credit Summary, line 4b;
- FTB 3806, Los Angeles Revitalization Zone Deduction and Credit Summary, line 4b; or
- FTB 3807, Local Agency Military Base Recovery Area Deduction and Credit Summary, line 4b.

f. Other (describe)

Reward from a crime hotline. Enter in column B the amount of a reward that was authorized by a government agency, that you 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.

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

Payments for alternative transportation (free or subsidized parking, alternative commute methods, monthly transit passes, etc.). Enter in column B the amount that you received from your employer, other than wages or salaries, for participating in an alternative transportation method and that is included in the amount on line 21 in column A. For more information, get FTB Pub. 1001.

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 this type of income that you included in the amount on line 21 in column A.

Rebates from water agencies or suppliers.

Enter in column B the amount of this type of income that you 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.

Qualified prizes with cash options. Enter in column C the lump-sum award or the value of an annuity awarded that was not included in federal gross income due to the special rule for cash options for receipt of qualified prizes.

Medical Savings Account (MSA) – If column A includes a taxable distribution from an MSA, you may owe additional tax on that amount. Get form FTB 3805P, Additional Taxes Attributable to IRAs, Other Qualified Retirement Plans, Annuities, Modified Endowment Contracts and MSAs.

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 27

Do not enter adjustments on these lines. California law is the same as federal law.

Line 28 – Self-employed Health Insurance Deduction

California law allows the deduction for self-employed health insurance. If you qualify for the federal deduction, you also qualify for the California deduction. However, the amount of the deduction will be different for California, and you must figure the deduction using the lower

California percentage of 40%. Complete the following worksheet to figure your California deduction and to make the necessary adjustment on Schedule CA (540):

1. Enter the total amount paid in 1998 for you, your spouse and dependents. Do not include amounts for any month you were eligible to participate in an employer-sponsored plan . . . 1 _____
2. Multiply line 1 by 40% (.40) . . . 2 _____
3. Enter your net profit and any other earned income from the business under which the insurance plan is established, minus any deductions you claim on Form 1040, line 27 and line 29 . . . 3 _____
4. Enter your federal self-employed health insurance deduction from Form 1040, line 28 4 _____
5. Enter the smaller of line 2 or line 3 5 _____
6. Subtract line 5 from line 4. Enter the result on line 28 in column B 6 _____

Line 29 and Line 30

Do not enter adjustments on these lines. California law is the same as federal law.

Line 31a – Alimony Paid

Enter the social security number and last name of the person to whom you paid alimony. **Note:** 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 – Add line 23 through line 31a 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 32. Enter the amount and "Form 2555" or "Form 2555-EZ" on the dotted line next to line 32.

Line 33 – Total

Subtract line 32 from line 22 in column B and column C.

Transfer the amount from line 33:

- Column B to Form 540, Side 1, line 14; and
- Column C to Form 540, Side 1, line 16.

If you plan to itemize deductions, go to Part II.

Caution: If Schedule CA (540), line 33:

Column B is a negative number, do not transfer it to Form 540, line 14. Instead, transfer the amount as a positive number to Form 540, line 16; or

Column C is a negative number, do not transfer it to Form 540, line 16. Instead, transfer the amount as a positive number to Form 540, line 14.

Part II – Specific Line Instructions

Line 35 – Federal Itemized Deductions

Enter the total amount of itemized deductions from your federal Schedule A, lines 4, 9, 14, 18, 19, 26 and 27. **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 35 through line 40.

Line 36 – State, Local and Foreign Income Taxes

Enter the state and local income tax from federal Schedule A, line 5 and only the portion relating to foreign income taxes from line 8. Include state disability insurance (SDI), limited partnership tax and income or franchise tax paid by S corporations.

Line 38 – Other Adjustments

Adoption-Related Expenses. If you deducted adoption-related expenses on your federal 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 38.

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 38.

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 38. 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 38.

Employee Business Expenses:

If you completed federal Form 2106, Employee Business Expense (or Form 2106-EZ), also complete Form 2106 (or Form 2106-EZ, Unreimbursed Employee Business Expenses) using California amounts. Specific differences between California and federal law are shown below.

- **Assets placed in service before 1/1/87:** Expenses on assets placed in service before 1/1/87 must be figured under California law; and
- **Federal employees on temporary duty status:** California did not conform to the recent 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 when completing Form 2106 (or Form 2106-EZ) using California amounts.

Compare line 10 on both Forms 2106 (or line 6 if using Forms 2106-EZ).

If the federal amount is larger, enter the difference as a negative number on line 38. If the California amount is larger, enter the difference as a positive number on line 38.

Investment Interest Expense. Your California deduction for investment interest expense may be different from your federal deduction. You must use form FTB 3526, Investment Interest Expense Deduction, to figure the amount to enter on line 38.

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 38.

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 38.

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 38.

Contribution of Appreciated Stock to a Private Foundation. For contributions made during 1998, enter the difference between the fair market value of the stock and the California basis as a negative number on line 38.

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 38.

Charitable Contribution Carryover Deduction. If you are deducting a prior year charitable contribution carryover, and the California carryover is larger than the federal carryover, increase your California itemized deductions by entering the additional amount as a positive number on line 38.

Line 40 – California Itemized Deductions

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

Single or married filing separate . . .	\$116,777
Married filing joint or	
qualifying widow(er)	\$233,556
Head of household	\$175,166

NO Transfer the amount from line 39 to line 40. Do not complete the worksheet below.

YES Complete the worksheet that follows.

Itemized Deductions Worksheet

1. Amount from Schedule CA (540), line 39. 1 _____
2. Using California amounts, add the amounts on federal Schedule A, line 4, line 13 and line 19 plus any gambling losses included on line 27 2 _____
3. Subtract line 2 from line 1 . . . 3 _____
Note: If -0-, stop. Enter the amount from line 1 on Schedule CA (540), line 40.
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 -0- or less, stop. Enter the amount from line 1 on Schedule CA (540), line 40.
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 40. 10 _____

Instructions for Form FTB 3885A

Depreciation And Amortization Adjustments

General Information

California legislation enacted in 1998 conforms California tax law to the Internal Revenue Code (IRC) as of January 1, 1998. However, there are continuing differences between California and federal tax law. California has not conformed to the changes made to the IRC by the Internal Revenue Service (IRS) Restructuring and Reform Act of 1998 (Public Law 105-206) and the Tax and Trade Relief Extension Act of 1998 (Public Law 105-277). Get FTB Pub. 1001, Supplemental Guidelines to California Adjustments, for more information on differences between California and federal law for the following items:

Expense treatment for small business (IRC Section 179): The maximum allowed under California law is \$16,000; the maximum allowed under federal law is \$18,500. **Amortization of certain intangibles (IRC Section 197):** Property classified as Section 197 property under federal law is also Section 197 property for California purposes. There is no separate California election required or allowed. However, for Section 197 property acquired before 1/1/94, the California adjusted basis as of 1/1/94, must be amortized over the remaining federal amortization period. **Qualified Indian reservation property:** California has not conformed to the accelerated recovery periods available under the Alternative Depreciation System (ADS) for such property. **Grapevines subject to Phylloxera or Pierce's disease:** For California purposes, replacement grapevines may be depreciated using a recovery period of 5 years instead of 10 years.

Purpose

Use form FTB 3885A to figure the adjustment for the difference between the amount of depreciation and amortization allowed as a deduction using California law and the amount allowed as a deduction using federal law. California law and federal law have not always allowed the same depreciation methods, special credits or accelerated write-offs. As a result, the recovery periods or the basis on which the depreciation is figured for California may be different from the amounts used for federal purposes. You will probably have reportable differences if all or part of your assets were placed in service:

- **Before 1/1/87.** California did not allow depreciation under the federal accelerated cost recovery system (ACRS), and you must continue to figure California depreciation for those assets in the same manner as in prior years.
- **On or after 1/1/87.** California provides special credits and accelerated write-offs that affect the California basis of qualifying assets. California did not conform to all changes to federal law enacted in 1993, and this causes the California basis or recovery periods to be different for some assets.

Differences may also occur for other less common reasons, and the instructions for Schedule CA (540 or 540NR) list them on the line for the type of income likely to be affected. For example, the instructions for Schedule CA (540 or 540NR), line 12, Business Income, list other adjustments you may need to report on form FTB 3885A if you are a sole proprietor. You may also get FTB Pub. 1001 for more information about figuring and reporting these adjustments.

If you are reporting differences for assets related to a passive activity, get form FTB 3801, Passive Activity Loss Limitations, for more information about passive activities.

Do not use form FTB 3885A to report depreciation expense from federal Form 2106, Employee Business Expenses. See the instructions for Schedule CA (540 or 540NR), line 38.

Specific Line Instructions

Note: Prepare and file a separate form FTB 3885A for each business or activity on your return that has a difference between California and federal depreciation or amortization. Enter the name of the business or activity in the space provided at the top of the form. If you need more space, attach additional sheets. However, complete Part II, Election to Expense Certain Tangible Property (IRC Section 179), only once.

Part I Identify the Activity as Passive or Nonpassive

Line 1 – Check the box to identify the activity as passive or nonpassive. A passive activity is any activity involving the conduct of any trade or business in which you did not materially participate. Get form FTB 3801 for more information.

If the activity is passive, use this form as a worksheet to figure the depreciation adjustment to carry to form FTB 3801. **Caution:** Beginning in 1994, and for federal purposes only, rental real estate activities of persons in real property business are not automatically treated as passive activities. California did not conform to this provision.

Part II Election To Expense Certain Tangible Property

You may elect to expense part of the cost of depreciable personal property used in your trade or business and certain other property described in federal Pub. 946, How to Depreciate Property. To do so, you must have purchased property, as defined in the IRC Section 179(d)(2), and placed it in service during 1998, or have a carryover of unused cost from 1997. If you elect this deduction, you must reduce your California depreciable basis by the IRC Section 179 expense. The maximum Section 179 expense allowed under California law is \$16,000.

Complete the worksheet below to figure IRC Section 179 expense for California. Include all assets qualifying for the deduction because the limit applies to all qualifying assets as a group rather than to each asset individually. **Refer to federal Form 4562 for information.**

1	Maximum dollar limitation for California	1	\$16,000
2	Enter total cost of Section 179 property placed in service during the tax year	2	
3	Threshold cost of Section 179 property before reduction in limitation	3	\$200,000
4	Reduction in limitation. Subtract line 3 from line 2. If zero or less, enter -0-	4	
5	Dollar limitation for tax year. Subtract line 4 from line 1. If zero or less enter -0-	5	
(a) Description of property		(b) Cost	(c) Elected cost
6			
7	Total elected cost of Section 179 property. Add column (c), line 6	7	
8	Tentative deduction. Enter the smaller of line 5 or line 7	8	
9	Carryover of disallowed deduction from 1997	9	
10	Enter the smaller of business income (not less than -0-) or line 5	10	
11	Section 179 expense deduction for California. Add line 8 and line 9, but do not enter more than line 10. Also enter the result on FTB 3885A, line 2	11	
12	Carryover of disallowed deduction to 1999. Add line 8 and line 9. Subtract line 11 from the result.	12	

Part III Depreciation

Line 3 – Complete column (a) through column (f) for each tangible asset or group of assets placed in service during the tax year. Be sure to use the California basis for assets on which you elected to take the Section 179 deduction. It will be the difference between line 6, column (b) and line 6, column (c) of the worksheet in Part II.

Line 8a and Line 8b – Are you using this form as a worksheet in connection with form FTB 3801?

Yes. Enter the amount from line 8a or line 8b on form FTB 3801, Side 2, California Passive Activity Worksheet, column (e).

No. Include the amount from line 8a on Schedule CA (540 or 540NR) in column B on line 12 for federal Schedule C activities; on line 17 for federal Schedule E activities; and on line 18 for federal Schedule F activities. Include the amount from line 8b on Schedule CA (540 or 540NR) in column C on line 12 for federal Schedule C activities; on line 17 for federal Schedule E activities; and on line 18 for federal Schedule F activities.

Part IV Amortization

Line 9 – Complete column (a) through column (f) for intangible assets placed in service during the tax year. Be sure to use the California basis and the California recovery period.

Line 14a and Line 14b – Are you using this form as a worksheet in connection with form FTB 3801?

Yes. Enter the amount from line 14a or line 14b on form FTB 3801, Side 2, California Passive Activity Worksheet, column (e).

No. Include the amount from line 14a on Schedule CA (540 or 540NR) in column B on line 12 for federal Schedule C activities; on line 17 for federal Schedule E activities; and on line 18 for federal Schedule F activities. Include the amount from line 14b on Schedule CA (540 or 540NR) in column C on line 12 for federal Schedule C activities; on line 17 for federal Schedule E activities; and on line 18 for federal Schedule F activities.

Instructions for California Schedule D

California Capital Gain Or Loss Adjustment

General Information

California legislation enacted in 1998 conforms California tax law to the Internal Revenue Code (IRC) as of January 1, 1998. However, there are continuing differences between California and federal tax law. California has not conformed to the changes made to the IRC by the Internal Revenue Service (IRS) Restructuring and Reform Act of 1998 (Public Law 105-206) and the Tax and Trade Relief Extension Act of 1998 (Public Law 105-277). For example, California does not conform to the federal reduced capital gains tax rates. California taxes capital gains at the same tax rate as other types of income.

Purpose

Use California Schedule D **only** if there is a difference between your federal capital gains and losses and your California capital gains and losses associated with the following:

- Gain on the sale of qualified small business stock which qualifies for the gain exclusion under IRC Section 1202;
- Disposition of property that was expensed or depreciated at some time during the period you owned it; California and federal depreciation and property expensing methods were different before 1987 and after 1/1/93 and caused a difference between the California and federal basis;
- 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;
- Distributed and undistributed capital gain dividends;
- Gain from involuntary conversion of capital assets not held for business profit; or
- Capital loss carryover from your 1997 California Schedule D.

For more information about the following, get FTB Pub. 1001:

- Disposition of property inherited before 1987;
- Disposition of S corporation stock acquired before 1987;
- Gain on the sale or disposition of a qualified assisted housing development to low-income residents or to specific entities maintaining housing for low-income residents; or
- Capital loss carryback.

Exclusion of Gain on Qualified Small Business Stock. California law (R&TC Section 18152.5) provides an exclusion (similar to the federal exclusion under IRC Section 1202) of 50% of the gain on the sale of qualifying small business stock originally issued after 8/10/93, and before 1/1/99, that was held for more than 5 years. However, for California purposes, 80% of the issuing corporation's payroll must be attributable to employment located within California, and, at least 80% of the value of the corporation's assets must be used by the corporation to actively conduct one or more qualified trades or businesses in California. See the Specific Line Instruction for Line 1b.

Installment Sales. If you sold property at a gain (other than publicly traded stocks or securities) and you will receive a payment in a tax year after the year of sale, you must report the sale on the installment method unless you elect not to do so. Get form FTB 3805E. Also use that form if you received a payment in 1998 for an installment sale made in an earlier year. **Note:** You may elect not to use the installment sale method for California by reporting the entire gain on Schedule D (or Schedule D-1 for business assets) in the year of the sale and filing your return on or before the due date.

At-Risk Rules and Passive Activity Limitations. If you dispose of (1) an asset used in an activity to

which the at-risk rules apply, or (2) any part of your interest in an activity to which the at-risk rules apply, and you have amounts in the activity for which you are not at risk, get and complete federal Form 6198, At-Risk Limitations, using California amounts to figure your California deductible loss under the at-risk rules. Once a loss becomes allowable under the at-risk rules, it becomes subject to the passive activity rules. Get form FTB 3801, Passive Activity Loss Limitations, to see how to report capital gains and losses from a passive activity.

Specific Line Instructions

Note: If you have gain on the sale of qualified small business stock that qualifies for the federal Section 1202 exclusion, go to the instructions for line 1b.

Line 1a – List each capital asset transaction.

Column (a) – Description of Property. Describe the asset you sold or exchanged.

Column (b) – Sales Price. Enter in this column either the gross sales price or the net sales price. If you received a Form 1099-B, 1099-S or similar statement showing the gross sales price, enter that amount in column (b). However, if box 2 of Form 1099-B indicates that gross proceeds less commissions and option premiums were reported to IRS, enter that net amount in column (b). If you entered the net amount in column (b), do not include the commissions and option premiums in column (c).

Column (c) – Cost or Other Basis. In general, the cost or other basis is the cost of the property plus purchase commissions and improvements minus depreciation, amortization and depletion. Enter the cost or adjusted basis of the asset for California purposes. Use your records and California tax returns for years before 1987 to determine the California amount to enter in column (c). If you used an amount other than cost as the original basis, your federal basis may be different from your California basis. Other reasons for differences are:

Depreciation Methods and Property Expensing California law: Did not allow the use of ACRS before 1987; Did not allow the use of an asset depreciation range 20% above or below the standard rate; Limits expensing of property under IRC Section 179 to \$16,000; Permitted rapid write-off of property such as solar energy systems, pollution control devices and property used in an EZ, the LARZ or LAMBRA.

Inherited Property – The California basis of property inherited from a decedent is generally fair market value (FMV) at the time of death. If you acquired community property as a surviving spouse, get FTB Pub. 1039, Basis of Property – Decedent/Surviving Spouse, for more information.

S Corporation Stock – Prior to 1987, California law did not recognize S corporations and your California basis in S corporation stock may differ from your federal basis. In general, your California basis will be cost-adjusted for income, loss and distributions received after 1986, while your stock was California S corporation stock. Your federal basis will be cost-adjusted for income, loss and distributions received during the time your stock qualified for federal S corporation treatment.

Special Credits – California law authorizes special tax credits not allowed under federal law or computed differently under federal law. In many instances if you claimed special credits related to capital assets, you must reduce your basis in the assets by the amount of credit.

Other adjustments may apply differently to the federal and California basis of your capital assets. Figure the original basis of your asset using the California law in effect when the asset was acquired, and adjust it according to provisions of California law in effect during the period of your ownership.

Line 1b – Section 18152.5 Exclusion. If the gain qualifying for the IRC Section 1202 exclusion also qualifies for the California exclusion under R&TC Section 18152.5: Enter in column (a) "Section 18152.5 Exclusion." Complete column (b) and column (c) according to the instructions for line 1a. Enter in column (d) the amount of gain that qualifies for the California exclusion. Enter in column (e) the entire gain realized. **If the gain qualifying for the IRC Section 1202 exclusion does not qualify for the California exclusion:** Complete column (a), column (b) and column (c) according to the instructions for line 1a. Enter -0- in column (d) and enter the entire gain realized in column (e).

Line 3 – Capital Gain Distributions. If you receive federal Form 2439, Notice to Shareholder of Undistributed Long-Term Capital Gains, from a mutual fund, do not include the **undistributed** capital gain dividends on Schedule D. If you receive federal Form 1099-DIV, Dividends and Distributions, enter the amount of **distributed** capital gain dividends.

Line 6 – 1997 California Capital Loss Carryover. Enter the amount of your 1997 California net capital loss that was more than the loss limitation.

Line 8 – Net Gain or Loss. If the amount on line 4 is more than the amount on line 7, subtract line 7 from line 4. Enter the difference as a gain on line 7.

If the amount on line 7 is more than the amount on line 4, subtract line 4 from line 7 and enter the difference as a loss on line 8.

Use the worksheet on this page to figure your capital loss carryover to 1999.

Line 9 – If line 8 is a net capital loss, enter the smaller of the loss on line 8 or \$3,000 (\$1,500 if you are married filing a separate return).

Line 12a – Enter the difference on line 12a and on Schedule CA (540 or 540NR), line 13, column B.

FOR EXAMPLE:

Loss on line 10 is less than loss on line 11.

Federal loss on line 10 is	\$1,000
California loss on line 11 is	\$2,000
Subtract line 10 from line 11.	\$1,000

Gain on line 10 and loss on line 11.

Federal gain on line 10 is	\$3,000
California loss on line 11 is	\$3,000
Add line 10 and line 11	\$6,000

Line 12b – Enter the difference on line 12b and on Schedule CA (540 or 540NR), line 13, column C.

FOR EXAMPLE:

Loss on line 10 is more than loss on line 11.

Federal loss on line 10 is	\$2,000
California loss on line 11 is	\$1,000
Subtract line 11 from line 10.	\$1,000

Loss on line 10 and gain on line 11.

Federal loss on line 10 is	\$2,000
California gain on line 11 is	\$5,000
Add line 10 and line 11	\$7,000

California Capital Loss Carryover Worksheet

1. Loss from Schedule D, line 11, stated as a positive number 1 _____
2. Amount from Form 540 or Form 540NR, line 17 2 _____
3. Amount from Form 540 or Form 540NR, line 18 3 _____
4. Subtract line 3 from line 2. If less than zero, enter as a negative amount. 4 _____
5. Combine line 1 and line 4. If less than zero, enter -0- 5 _____
6. Loss from Schedule D, line 8 6 _____
7. Enter the smaller of line 1 or line 5 7 _____
8. Subtract line 7 from line 6. This is your capital loss carryover to 1999 8 _____