

Practical Guide to California Taxes: The Impact of Economic Crisis

reviewed by Robert W. Wood

Full Text Published by **taxanalysts**[®]

* * * * *

Robert W. Wood is a tax lawyer with a nationwide practice. The author of more than 30 books including Taxation of Damage Awards & Settlement Payments (4th Ed. 2009) (available at www.taxinstitute.com), he can be reached at wood@woodporter.com.

This discussion is not intended as legal advice and cannot be relied on for any purpose without the services of a qualified professional.

Practical Guide to California Taxes: The Impact of Economic Crisis (ISBN 978-0-8080-2380-7) by Kathleen K. Wright is available for \$109 from CCH Wolters Kluwer at <http://onlinestore.cch.com>.

Everyone knows California is in dire straits. Among California tax professionals, less recent but equally pervasive news is that resolving California tax problems is almost always harder than resolving federal ones. That is because of a variety of factors, not the least of which is the lack of a deal-making attitude prevailing at California's taxing agencies -- the Franchise Tax Board and the State Board of Equalization. But whatever the cause, practitioners and the public alike know that California needs money, and tax revenue has to go up. Soon.

In this still golden but decidedly unhappy milieu, the new CCH paperback titled *Practical Guide to California Taxes: The Impact of Economic Crisis* is worth reading and keeping as a reference. Prof. Kathleen K. Wright of California State University, Fullerton (aided by contributing authors Craig Morris, Benedict Cabaltica, Abner Chong, and Mariela Kim), has done an admirable job of covering many basics with a special focus on California's current plight.

The book begins with an overview chapter about California's response to the recession. In one 15-page-long bullet, readers get an assessment of where the state is now and where it is going. But this is no mere theoretical discussion; the book is filled with changes in the offing that affect the alternative minimum tax, apportionment, and more.

Chapter 2 (also about 15 pages) gives basic rules and rates for individuals, including estimated payments, backup withholding, and so forth. Chapter 3 covers corporate tax rates and payments, including estimated payment issues, penalties, and safe harbors. This is an ideal discussion for accountants occasionally dabbling in California and for businesses needing an overview.

And then there are credits. Chapter 4 includes over 20 pages of discussion, some of it quite detailed, about available credits in California. Apart from the usual suspects,

there's a good discussion of the new small-business hiring credit (sections 17053.80 and 23623 of the California Revenue and Taxation Code) and of the film credit (sections 17053.85 and 23685). Those are both significant credits, and the discussion is thorough and alone worth the price of the book.

Conformity and More

Chapter 5 starts with an age-old problem in California: conformity to federal tax law. This discussion is both complete and summary in nature, which is difficult to do. It would be hard to find this much practitioner-oriented conformity discussion anywhere else. My only complaint is that there has been a little additional conformity since publication of the book (although I understand the next edition will update that).

Chapter 6 covers nexus, a difficult topic for everyone and an ever-present concern in businesses tiptoeing through the Golden State. "Nexus" is a word that can strike fear into the hearts of business executives hoping to sell products or provide services in California. Unfortunately, nexus is also one of those tax subjects that everyone seems to think they know something about. There is often a danger of getting so close to the trees that one cannot see the forest.

And that is where this book shines. In about 35 pages, it gives an overview of what nexus is all about, critical U.S. Supreme Court decisions, the different kinds of nexus, and the implications for sales and use taxes and for franchise and income taxes. And there is more. There is a nice discussion of intangible holding-company issues, including the case law supporting the use of intangible holding companies as a way to reduce state taxes.

The idea, of course, is to set up an intangible holding company in Delaware or another low-tax state as a way of isolating intangible assets and protecting them from higher taxes. Typically, those assets would include trademarks, trade names, loans, rental agreements, and other licensing agreements. The holding company would then enter into agreements with subsidiaries or affiliates in California and other high-tax states. If there is a weakness in this book's discussion, it is that the focus is on other states, because California -- given its combined reporting system -- has not been aggressive on those structures.

Yet the book is appropriate in its few-page discussion of all of the many cases on holding-company issues around the country, plus the states' response of addback statutes. Although California does not have an addback statute because of its unitary method and combined reporting, there is a nice discussion of how California's system and addback statutes in other states can be traps for multistate businesses. Since almost anyone reading the *Practical Guide* doubtless will be operating in multiple states, this multistate approach to the subject matter is both intuitive and practical.

Of course, this is primarily a California book, and it appropriately spends considerable time with California's peccadilloes over nexus, including California's new definition of doing business that takes effect in 2011. Many business people, not to mention tax advisers, would benefit from reading at least those pages of the book.

Another aspect of the book's comprehensive outlook is a discussion of Public Law 86-272 and the California cases interpreting that federal mandate. The discussion then segues into the treatment of nonresident partners and the tax problems they face in California. That subject is really important in practice, and this is a practical and straightforward discussion. In its eight pages, it even distinguishes between the treatment nonresident partners receive and the subtle differences experienced by shareholders of an S corporation or members of a limited liability company.

Chapter 7 might be regarded as only for accountants, but that would be a mistake. It covers allocation and apportionment and the property and payroll factors. Appropriately, the sales factor is covered separately in Chapter 8. Together, those two chapters fill about 65 pages, which is sufficient in scope and detail. One can focus on some of the trees, yet at the same time get a good view of the forest.

This is a complex subject, and the author has presented how and why those apportionment factors are at play, both nationally and in California. One of the great features of those chapters is their baseline treatment of the issue nationally, with descriptions of the unique features of California law. Anyone reading this book or using it as a reference (for it is appropriate to use in both ways) will almost certainly be operating or advising clients in multiple states. This may not be the most detailed treatment of these subjects, but plenty of planning ideas are presented with examples that make the book a bargain.

Chapter 9 deals with enterprise zones, which, although generally uninteresting to me, would certainly be interesting to any business trying to capitalize on them. And there are now so many of them in California (42 at last count!). There's even a brief reference to the armies of consultants now available to be retained to study taxpayer businesses to determine eligibility for any of the benefits in this ever-expanding bevy of credits. (I may need to start doing this kind of work after all.)

Chapter 10 covers sales and use taxes with a brief but succinct discussion of the basic rules. Given the multistate bent of the book, it segues back to nexus issues in sales tax cases. There is a topical discussion of Borders, Barnes & Noble, and Amazon.com; where the law is currently; and where it is going.

Conclusion

All in all, Wright's *Practical Guide to California Taxes: The Impact of Economic Crisis* is worth far more than its list price. Taxes are complex and difficult to understand, even for professionals. California taxes are worse, *way* worse, than federal ones. As professionals (whether lawyers or accountants), we are often looking at a particular issue, not at the overall landscape.

This book manages to present a vast Golden State expanse -- a veritable Oregon-to-Mexico tax reprise -- in a readable and compact form. Although its subtitle *The Impact of Economic Crisis* may be a marketing hook, it's true that the whole system is changing radically -- and one of the most important changes is the development of the new nexus rules starting in 2011. Get a copy. In fact, get several. Any clients operating in California -- or even thinking of operating there -- should get one too.