

# State of California — Franchise Tax Board

## Guidelines for Filing a Group Form 540NR

FTB Pub. 1067

This publication is for S corporations, partnerships, and limited liability companies (LLCs) that elect to file a group nonresident return. In this publication the term “*business entity*” refers to any one of these entities. The term “*individual*” refers to a shareholder, partner, or member who is a natural person and their spouse.

### What's New

**Shareholder's Income:** A shareholder's pro-rata share of income from an S-corporation is treated the same as a partner's distributive share of income from a partnership. The income is treated as if it was realized directly from the source. Income from California sources is subject to California tax law. *Valentino et. al. v. Franchise Tax Board* (CtApp. March 23, 2001) 105 Cal. Rptr. 2d 304.

#### Credits Available:

- Solar Energy System Credit is available from January 1, 2001 until January 1, 2006.
- Joint Strike Fighters Credit is available as of January 1, 2001.

#### Amended/Extended Credits:

- The Employer Child Care Program Credit and the Employer Child Care Contribution Credit are extended until January 1, 2007.
- The Community Development Financial Institution Investments Credit was extended until January 1, 2007. Changes to the credit include renaming “qualified deposits” to “qualified investments” and defining “qualified investments,” limiting the eligible investment amount, and requiring Franchise Tax Board to advise and assist in the administration of the credit.

**Income Exclusion:** Amounts received as rebates or vouchers from a local water agency, energy agency or energy supplier for the purchase and installation of water conservation appliances and devices are excludable from income.

**Reference Change:** Any references to Bank and Corporation Tax Law (B&CTL) is changed to Corporation Tax Law (CTL) as of January 1, 2001.

**Napa Valley Losses:** The losses sustained as a result of the 2000 Napa Valley earthquakes can be carried forward at 100% for 5 years, then the remaining balance can be carried forward an additional 10 years at 55%.

**Nonresident Returns:** For the 2001 tax year, a new form is available for nonresidents and part-year residents, Short Form 540NR, California Nonresident or Part-year Resident Income Tax Return. The Short Form 540NR is for nonresident and part-year taxpayers who have limited income sources and deductions. The Form 540NR name has been changed to Long Form 540NR, California Nonresident or Part-year Resident Income Tax Return. References to the Form 540NR in this booklet mean the Long Form 540NR.

### A Introduction

California allows certain nonresident individuals that receive distributive shares of income from business entities that derive income from California sources or are doing business in California to elect to file group nonresident returns (Revenue and Taxation Code (R&TC) Sections 18535 and 23810). The business entity files the group nonresident return and pays the tax on behalf of the electing non-resident individuals.

The business entity must use Form 540NR, for the group nonresident return. The return must be for a calendar year and include at least two electing nonresident individuals. Special instructions for completing Form 540NR are explained in Section N, Instructions for Completing Group Nonresident Return of this publication.

### B Why File a Group Nonresident Return?

A group nonresident return is filed on behalf of the electing nonresident individuals for their convenience. When filing an individual return, a nonresident must report all income from all sources in addition to the California source income. On the group nonresident return, only the California source income from the business entity is reported. The income is taxed at the highest personal income tax marginal rate. The highest marginal rate is 9.3%.

### C Who Can Be Included in the Group Nonresident Return?

To be included in the group nonresident return:

- The shareholder/partner/member must be an individual. Estates, trusts, partnerships, LLCs, C corporations, or S corporations cannot be included in the group nonresident return;
- The individual must be a full-year nonresident of California; **and**
- The only California source income of the electing nonresident individual must be from the business entity. However, a nonresident individual can be included on more than one group nonresident return.

### D Individual's Decision to be Included in the Group Nonresident Return

Each nonresident individual must decide whether to be included in the group nonresident return prior to its filing. Once the group nonresident return is filed, it cannot be amended to either include or exclude a nonresident individual.

Similarly, if an electing nonresident individual is included in the group nonresident return, the individual may not subsequently file an individual nonresident return, unless the individual discovers that he or she has income from other California sources and therefore would not qualify to participate in a group nonresident return.

The business entity is responsible for allowing each nonresident individual the annual option of being included in the group nonresident return. To assist individuals in making an informed decision about the implications of inclusion in the group nonresident return, the business entity must inform the nonresident individuals of the terms and conditions of filing a group return specified on form FTB 3864, Group Nonresident Return Election.

### E Election to File a Group Nonresident Return

The business entity makes an annual election to file a group nonresident return on behalf of the electing nonresident individuals. Once made, the election is irrevocable for the taxable year. Complete form FTB 3864 (included in this publication), to make the election and attach it to the Form 540NR filed for the group.

### F Requirement for the Electing Individual to File a California Income Tax Return

The requirement to file a California personal income tax return is determined on an individual basis. See “Do I Have to File?” in the Form 540NR Tax Booklet.

For 2001, a full-year nonresident is required to file a return if the individual has any California source income and has more than \$11,901 gross income from all sources or more than \$9,521 adjusted gross income from all sources, or owes \$1 or more of tax. For prior years, get the Form 540NR Tax Booklet for the appropriate year.

## G Reporting of Gains/Losses

**Capital Gains/Losses.** All limitations normally applied at the individual level apply on the nonresident group return. For instance, an individual's California source capital losses from a business entity may only be deducted to the extent of California source capital gains, plus \$3,000. The allowable capital loss for each electing nonresident is totaled and entered on the return. The filing status of nonresident electing individuals is deemed to be single, limiting each to a \$3,000 capital loss. The business entity must keep track of the allocable share of the California source capital gains and losses (including carryovers) for each electing nonresident individual.

**Internal Revenue Code (IRC) Section 1231 net losses** are allowed in full.

**Passive Losses.** The business entity must complete a single form FTB 3801, Passive Activity Loss Limitations, for the electing nonresident individuals included in the group return. Only California source passive losses are reported on form FTB 3801. Passive losses will be allowed only to the extent of passive income. When losses are not allowed, they are suspended at 100% for each electing nonresident individual. When suspended passive losses are released by current year passive income, the suspended prior year losses offset the current year passive income on the group return. Suspended prior year losses are also released upon disposition of the entire interest in the passive activity. The business entity must keep track of the allocable share of the suspended California source passive losses for each electing nonresident individual included in the group return.

## H Individual Deductions Not Allowed on the Group Nonresident Return

**Individual deductions** are not allowed on the group nonresident return. Individual deductions include, but are not limited to, the deduction for self-employment tax, itemized deductions, and the standard deduction. However, there is an exception for the deduction for contributions to a deferred compensation plan. See Section I, Contributions to a Deferred Compensation Plan.

A **Net Operating Loss (NOL)** cannot be claimed on the group return. The NOL is an individual deduction limited to the taxpayer's overall loss taking into account worldwide income and deductions. An NOL is also limited by the individual's California source loss. See instructions for form FTB 3805V, Net Operating Loss (NOL) Computation and NOL and Disaster Loss Limitations — Individuals, Estates, and Trusts.

## I Contributions to a Deferred Compensation Plan

A deduction under IRC Section 401 through Section 424, as modified by California, is allowed on the group nonresident return. However, no deduction is allowed to any electing nonresident individual who has earned income from any other source.

The deduction is computed by multiplying the allowable federal deduction by the electing nonresident individual's California apportionment percentage.

## J Credits

Only credits directly attributable to the business entity's activities can be claimed on the group nonresident return, such as the low-income housing credit and the manufacturers' investment credit.

Individual credits, such as the personal, blind, senior, or dependent exemption credits and the other state tax credit, are not allowed on the group nonresident return. To use individual credits, the individual should file a separate Form 540NR and should not be included on the group return.

## K Estimated Tax Requirements

Generally, estimated tax payments are required if the group nonresident return's net tax after allowable tax credits is \$200 or more. If the tax is underpaid, a penalty for the underpayment of estimated tax will be assessed based on the net tax of the group nonresident return. Get Form 540-ES, Estimated Tax for Individuals, and form FTB 5805, Underpayment of Estimated Tax by Individuals and Fiduciaries, for more information.

## L How to Make Estimated Tax Payments on Form 540-ES

To make group nonresident return estimated payments:

1. Type or print the following information in the top margin of the Form 540-ES:  
GROUP FILING PROGRAM MS A-2  
ATTN IVS (732)
2. Enter the name and address as shown on page 4 of this publication.
3. Mail the estimate voucher with payment to the address shown on the Form 540-ES.

## M Moving Estimated Payments Between the Group Nonresident Return and the Individual Nonresident Return

If the business entity made estimated tax payments on behalf of a nonresident individual throughout the taxable year and the nonresident individual opts out of the group filing before the group return is filed, then the individual's distributive share of estimated tax payments may be moved to the individual's account and claimed on the individual's return. To move payments, fax, or mail a letter to:

GROUP FILING PROGRAM MS A-2  
ATTN INFORMATION VALIDATION SECTION (732)  
FRANCHISE TAX BOARD  
PO BOX 1468  
SACRAMENTO CA 95812-1468  
(FAX) (916) 845-0716

Include the following information in your letter:

1. Business entity's name;
2. Federal employer identification number (FEIN);
3. California Secretary of State (SOS) file number, if issued;
4. Individual's name;
5. Social security number;
6. Individual's address;
7. Estimated tax payments to be applied to each quarter;
8. Tax year;
9. Contact person and phone number; and
10. A statement indicating the tax identification number of the account the payment is to be moved from and the tax identification number of the account to receive the payment.

The letter should be signed by a general partner, member-manager, corporate officer, or an attorney-in-fact of the business entity.

Use the same procedure if the electing nonresident individual made individual estimated tax payments and subsequently elected to be included in the group nonresident return.

## N Instructions for Completing Group Nonresident Return

Complete the group nonresident return using personal income tax Form 540NR. Follow the instructions for the form with the following modifications:

1. Type or print the following information in the top margin of Form 540NR, Side 1:  
GROUP FILING PROGRAM MS A-2  
ATTN IVS (732)
2. If there is a mailing label on the front of the Form 540NR Tax Booklet, use the label. If you need to make any changes, cross out the incorrect information and clearly print the new information.  
If there is no mailing label, follow the example on page 4 for entering the name and address on the group nonresident return.
3. Complete and attach Schedule 1067A, Nonresident Group Return Schedule, to Form 540NR.
4. Complete "Step 1," "Step 1a," and "Step 2" as shown in the example on page 4. Skip line 6 through line 19. Enter the cumulative totals for all individuals included in Schedule 1067A, Part I, as follows:
  - a. Enter the total distributive share of California source income from Schedule 1067A, Part I, column (c), on line 25;
  - b. Enter the total California tax from Schedule 1067A, Part I, column (e) on line 27;
  - c. Enter the credit name, code number, and total amount of each type of credit on line 37 and line 38, if applicable;
  - d. Enter the total net tax from Schedule 1067A, Part I, column (g) on line 46; and
  - e. Complete the remaining lines of the Form 540NR as appropriate.
5. If an amount is due, make the check or money order payable to "Franchise Tax Board" for the full amount. Write the business entity's FEIN, SOS file number, and "2001 Group 540NR" on the check or money order.
6. Complete, sign, and attach form FTB 3864 to Form 540NR. The form FTB 3864 must be signed by an authorized person or attorney-in-fact. Signing form FTB 3864 means the business entity and all the electing individuals agree to the terms and conditions for filing a group nonresident return.
7. Mail the group nonresident return using one of the appropriate addresses shown in Step 11. Also attach a copy of the form to the business entity's return.  
If you lease a private mailbox (PMB) from a private business rather than from the United States Postal Service, include the box number in the field labeled "PMB no." in the address area of form FTB 3864 and the Form 540NR.

## O Special Information for Partnerships and LLCs Subject to Apportionment

Title 18, Cal. Code Reg. Section 17951-4 applies to the income computation of the nonresident partners/members of a partnership/LLC. The regulation provides that 100% of the nonresident's distributive share of the partnership's business income plus any guaranteed payment, is subject to apportionment. Guaranteed payments are treated as part of a partner's distributive share of partnership business income. See R&TC Section 17854.

If the partnership qualifies as an investment partnership under R&TC Section 17955(c), generally the dividends, interest, gains, and losses from that partnership will be sourced in the partner's/member's state of residence. For more information, see instructions for Form 565, Partnership Return of Income, or Form 568, Limited Liability Company Return of Income.

If the partnership does not qualify as an investment partnership under R&TC Section 17955(c) or if the partnership does qualify as an investment partnership but the partner/member is disqualified under R&TC Section 17955(b), pertaining to investment activities interrelated with trade or business within this state, then the normal apportionment and allocation rules apply in determining the character of the income as business or nonbusiness. Business income should be apportioned using the partnership factors. Nonbusiness income from intangibles should generally be allocated to each partner's/member's state of residence.

## P Withholding Requirements of Partnership/LLC

Withholding is required if:

- California source income is allocable under IRC Section 704 to a foreign nonresident partner/member; or
- California source income distributed to a domestic (nonforeign) nonresident partner/member exceeds \$1,500 in the calendar year.

The withholding rates are 8.84% for foreign corporate partners/members, 9.3% for foreign nonresident individual partners/members, and 7% for all domestic nonresident partners/members. Withholding is not required if the partner/member has received authorization waiving the withholding from the Franchise Tax Board. However, there is no provision in the tax law to allow a waiver of withholding for a foreign nonresident partner/member.

For additional information concerning California withholding requirements, please see FTB Pub. 1016, Nonresident Withholding Real Estate Guidelines; FTB Pub. 1017, Nonresident Withholding Partnership Guidelines; FTB Pub. 1023, Nonresident Withholding Independent Contractor Rent and Royalty Guidelines; or call the Nonresident Withholding Section's automated toll-free telephone service at (888) 792-4900.

## Q Additional Information

Address correspondence regarding the group nonresident return to:

GROUP FILING PROGRAM MS A-2  
ATTN INFORMATION VALIDATION SECTION (732)  
FRANCHISE TAX BOARD  
PO BOX 1468  
SACRAMENTO CA 95812-1468

**Caution:** DO NOT mail Form 540NR or Form 540-ES to this address. Mail Form 540NR and Form 540-ES to the address shown on each form.

The telephone number for information on the group nonresident return is: (916) 845-3465.

**Forms by Internet** – You can download, view, and print California tax forms and publications. Go to our Website at: [www.ftb.ca.gov](http://www.ftb.ca.gov)

Access other state agencies' websites through the State Agency Index on California's Website at: [www.ca.gov](http://www.ca.gov)

**Forms by Phone and Mail** – See back cover of the Form 540NR Tax Booklet or the business entity tax booklet for the phone number and address to order California tax forms and publications.

TAXABLE YEAR

Enter Entity  
FEIN

CALIFORNIA FORM

2002 Estimated Tax for Individuals

Due June 17, 2002

540-ES

Fiscal year filers, enter year ending month: Year 2003

Your first name * A o r C		Initial	Last name * * P T S P o r S G N F		Your social security number 1 2 3 4 5 6 7 8 9								
If joint payment, spouse's first name		Initial	Last name		Spouse's social security number								
Present home address — number and street, PO Box, or rural route C / o E N T I T Y N A M E & A D D R E S S					Apt. no.		PMB no.		Payment Voucher 2				
City, town, or post office E N T I T Y C I T Y , T O W N					State		ZIP Code						

Do not combine this payment with payment of your tax due for 2001. Make your check or money order payable to "Franchise Tax Board." Write your social security number and "Form 540-ES 2002" on it. Mail this voucher and your check or money order to: **FRANCHISE TAX BOARD, PO BOX 942867, SACRAMENTO CA 94267-0031**

If No Payment is Due, Do Not Mail This Form.

Amount of payment

For Privacy Act Notice, get form FTB 1131.

540ES02103

Form 540-ES (REV. 2001)

✂ — DETACH HERE — — — — — IF NO PAYMENT IS DUE, DO NOT MAIL — — — — — DETACH HERE — ✂

California Nonresident or Part-Year  
Resident Income Tax Return 2001

Long Form

FORM

540NR

Fiscal year filers only: Enter month of year end: month year 2002.

Step 1 Place label here or print  Name and Address	Your first name * A o r C		Initial	Last name * * P T S P o r S G N F		PBA Code		P  A C  R  P	
	If joint return, spouse's first name		Initial	Last name					
	Present home address — number and street, PO Box, or rural route C / o E N T I T Y N A M E & A D D R E S S					Apt. no.			PMB no.
	City, town, or post office E N T I T Y C I T Y , T O W N					State			ZIP Code
Step 1a SSN	Your social security number 1 2 3 4 5 6 7 8 9				Spouse's social security number				IMPORTANT: Your social security number is required.

Step 2 Filing Status  Fill in only one.	1 <input checked="" type="radio"/> Single
	2 <input type="radio"/> Married filing joint return (even if only one spouse had income)
	3 <input type="radio"/> Married filing separate return. Enter spouse's social security number above and full name here _____
	4 <input type="radio"/> Head of household (with qualifying person). STOP. See instructions.
	5 <input type="radio"/> Qualifying widow(er) with dependent child. Enter year spouse died _____

Enter Entity  
FEIN

\* enter A if partnership or LLC,  
enter C if S corporation

\*\* enter PTSP if partnership or  
LLC, enter SGNF if S corporation

2001 Nonresident Group Return Schedule

1067A

Attach this schedule to your California group Form 540NR.

S Corporation/Partnership/Limited Liability Company name

Federal employer identification no. (FEIN)

DBA

CA Corporation or Secretary of State file no.

## Part I Electing Nonresident Individuals (Shareholders/Partners/Members) Included in the Group Nonresident Return (Use additional sheet(s) if necessary)

**Note: Column (a) and (b) –** If the nonresident individual has a spouse, include the spouse's information in both columns.

**Column (d)** – Amount of deferred compensation deduction. See FTB Pub. 1067, Section I, for more information.

**Column (f)** – Tax credit allowable. See FTB Pub. 1067, Section J, for more information.

(a) Social security number (SSN)	(b) Name	(c) CA source income (Less deferred compensation, if any)	(d) Deferred compensation	(e) CA tax (col. (c) multi- plied by the highest marginal tax rate, 9.3%)	(f) Credit	(g) Net tax (col. (e) minus col. (f))
<b>Total</b> .....						

## Part II Individuals (Shareholders/Partners/Members) Not Included in the Group Nonresident Return (Use additional sheet(s) if necessary)

(a) Social security number (SSN)/FEIN	(b) Name	(c) CA source income
Total .....		

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## Group Nonresident Return Election

3864

Attach to Form 540NR and to the appropriate business entity return.

Business entity's name		Federal employer identification no. (FEIN)		CA Corp. or Secretary of State file no.	
Business address		PMB no.		Telephone	
				( )	
City or town, state, and ZIP Code				Nature of business activity	
Principal California business address				State in which the principal business activity is conducted	
				Shareholders/Partners/Members	
				Number non-electing	
				Number electing	

Form FTB 3864 is to be used by S corporations, partnerships, and limited liability companies (LLCs). The term *"business entity"* refers to any one of these entities, as appropriate. The term *"individual"* refers to the nonresident shareholder, partner, or member who is a natural person and their spouse.

**TERMS AND CONDITIONS OF FILING A GROUP NONRESIDENT RETURN**

The above business entity and its electing nonresident individuals included in the filing of the group nonresident return (Form 540NR) agree to the following terms and conditions:

- The election to file a group nonresident return on behalf of the electing nonresident individuals must be made annually by the business entity by completing this form. This form must be signed by an authorized general partner, member-manager, corporate officer, or an attorney-in-fact of the business entity.
- The group nonresident return must be a calendar year return.
- Form 540NR, California Nonresident or Part-Year Resident Income Tax Return, must be used for the group nonresident return. Form 540NR will be prepared as outlined in FTB Pub. 1067, Guidelines for Filing a Group Form 540NR.
- The business entity will provide to each nonresident individual the election to be included in the group nonresident return. The nonresident individual will make the election on an annual basis. The election to participate for a given year may be made only by an individual qualified to be included in a group nonresident return and is irrevocable upon the filing of the group nonresident return for that year.
- The business entity shall maintain a file of powers of attorney executed by each electing nonresident individual. The powers of attorney shall authorize the business entity to include the electing nonresident individual in the group nonresident return filed.
- There must be at least two electing nonresident individuals to file a nonresident group return.
- To be included in the group nonresident return, the electing shareholder/partner/member must be an individual and a full-year nonresident of California. Estates, trusts, partnerships, LLCs, C corporations, or S corporations cannot be included in the group nonresident return.
- To be included in the group nonresident return, the income from the business entity must be the only California source income of the individual, unless the other California source income is reported by the individual in another qualified group nonresident return filed under this provision.
- No deductions are allowed except those necessary to determine each individual's distributive share of income from the business entity. However, a deduction is allowed for contributions to qualified deferred compensation plans attributable to earned income of a partner/member as provided in Subchapter D of Chapter 1 of Subtitle A of the Internal Revenue Code (IRC), as modified by the Revenue and Taxation Code (R&TC) beginning with Section 17501. No deduction to a qualified deferred compensation plan is allowed if the individual has earned income from any other source. See FTB Pub. 1067.

- j. No credits are allowed except those directly attributable to the business entity's activity. In the event allowable credits exceed the amount of tax for a given year and credits are available for carryover, the business entity will properly account for such credit with respect to each individual included in the group nonresident return.
- k. Each individual included in the group nonresident return will be assessed tax on California source income at the highest individual marginal rate.
- l. The business entity shall make estimated tax payments for the group pursuant to R&TC Section 19136. Payments for the group will be made under the federal employer identification number (FEIN) of the business entity.
- m. The business entity shall receive any notices of proposed tax to be assessed and any assessments of tax with respect to the group nonresident return. Additionally, the business entity, or its designated representative, shall represent the individuals in protest, claims for refund, appeal procedures, or in court proceedings related to tax matters associated with the group nonresident filing. The business entity shall pay any tax assessments and any attributable interest and penalties for the group nonresident return. The penalties will be computed as if all the electing individuals included in the return did not participate in any other group nonresident return for that same tax year. The business entity's agreement to pay tax, interest, and penalties does not absolve the individuals of their respective obligations to pay their California taxes, interest, and penalties, if such obligations are not satisfied by the business entity.
- n. If an electing nonresident individual has a tax deficiency attributable to California source income that was distributable by the business entity to the individual for any tax year, the business entity agrees that it shall act as a withholding agent. The business entity agrees to accept (without contesting jurisdiction) Orders to Withhold (OTW) against funds to be distributed to such individuals. The funds need not be paid over to the Franchise Tax Board until they are clearly identified as being currently distributable.
- o. The business entity shall file Form 100S, California S Corporation Franchise or Income Tax Return/Form 565, California Partnership Return of Income/Form 568, Limited Liability Company Return of Income, as appropriate. A business entity doing business within and outside of California must determine the portion of the total net income that has its source in California using the allocation and apportionment provisions in the Uniform Division of Income for Tax Purposes Act (UDITPA). Refer to R&TC Sections 25120 through 25141 and applicable regulations.

The terms and conditions set forth above are agreed to on behalf of the above-named business entity and its electing nonresident individuals. I have been authorized by the above-named business entity and its electing individuals to accept the terms and conditions set forth above.

Authorized signature (As specified in item a.)

Title

Date

Telephone

▶

( )

Print name

Business entity's name

▶

▶