

Supplemental Guidelines to California Adjustments

General Information

In general, California law conforms to the Internal Revenue Code (IRC) as of January 1, 2001. However, there are continuing differences between California and federal law. It should be noted that California does not always conform to the entire provisions of a public law. California has conformed to some of the changes made to the IRC after January 1, 2001, including some provisions of the Economic Growth and Tax Relief Reconciliation Act of 2001 (Public Law 107-16), the Victims of Terrorism Tax Relief Act of 2001 (Public Law 107-134), and the Job

Creation and Worker Assistance Act of 2002 (Public Law 107-147). California has not conformed to any of the provisions of the Jobs and Growth Tax Relief Reconciliation Act of 2003 (Public Law 108-27) and the Military Family Tax Relief Act of 2003 (Public Law 108-121).

Purpose

Use these guidelines to make adjustments to federal adjusted gross income that are necessary because of current year or prior year differences between California and federal law. Generally, you report these adjustments directly on Schedule CA

(540), California Adjustments — Residents, or Schedule CA (540NR), California Adjustments — Nonresidents or Part-Year Residents. If you are required to make multiple adjustments for any one line on Schedule CA (540 or 540NR), attach a schedule to your return summarizing these adjustments.

In some cases you need to complete other forms or schedules to figure the adjustment to carry to Schedule CA (540 or 540NR). See "Order Forms and Publications" on the back cover of your tax booklet for information about ordering forms.

ITEM	DIFFERENCES BETWEEN FEDERAL AND CALIFORNIA LAW	WHAT TO DO FOR CALIFORNIA
Wages, Salaries, Tips, etc.		
• Military pay	Special rules apply to active duty military pay.	Get FTB Pub. 1032, Tax Information for Military Personnel, for more information.
• Sick pay received under the Federal Insurance Contributions Act and Railroad Retirement Act	California excludes from income the sick pay received under these Acts.	Enter qualifying sick pay included in federal income on Schedule CA (540 or 540NR), line 7, column B.
• Income exempted by U.S. treaties	Income exempted by treaty under federal law may be excluded for California only if the treaty specifically excludes the income for state purposes.	Enter the amount excluded from federal income on Schedule CA (540 or 540NR), line 7, column C.
• Employee income exclusions for ridesharing programs	Under federal law and the provisions administered by the Employment Development Department, qualified transportation benefits are excluded from gross income. Under the California Revenue and Taxation Code (R&TC), there are no monthly limits for the exclusion of these benefits and California's definitions are more expansive. Federal law provides an income exclusion for the value of parking provided to an employee up to \$190 per month and for transit passes provided to an employee up to \$100 per month. California law provides an income exclusion for compensation or the fair market value of other benefits (except for salary or wages) received for participation in a California ridesharing arrangement (subsidized parking, commuting in a third-party vanpool, a private commuter bus, a subscription taxipool, and monthly transit passes provided for employees and their dependents).	Enter the amount of ridesharing benefits received and included in federal income on Schedule CA (540 or 540NR), line 7, column B.
• California Qualified Stock Options (CQSOs)	California law provides an income exclusion for California qualified stock options (issued on or after 1/1/97 and before 1/1/02), that are exercised by an individual who has earned income for the taxable year from the corporation granting the CQSO of \$40,000 or less; and has exercised options for no more than 1,000 shares with a combined fair market value of less than \$100,000 (determined at the time the options are granted). Get FTB Pub. 1004, Stock Option Guidelines, for more information.	Enter on Schedule CA (540 or 540NR), line 7, column B the amount included in federal income that qualifies for the California exclusion.
• Medical expenses	California allows an exclusion from gross income for employer-provided accident, health insurance, and medical expense reimbursement for registered domestic partners and that partner's dependents if they were not previously deducted. Self-employed individuals may also claim a deduction for health insurance costs paid for registered domestic partners and the partner's dependents.	Enter on Schedule CA (540 or 540NR), line 7, column B the amount included in federal income.

ITEM	DIFFERENCES BETWEEN FEDERAL AND CALIFORNIA LAW	WHAT TO DO FOR CALIFORNIA
Earnings of American Indians	Federal law taxes income received by Indians from reservation sources. California does not tax income earned by tribal members who live in Indian country affiliated with their tribe and receive earnings from the same tribal source of which they are a member. Get FTB 674, Frequently Asked Questions About the Income Taxation of American Indians, for more information.	Enter on Schedule CA (540 or 540NR), line 7, column B the earnings included in federal income that are exempt for California.
Clergy housing exclusion	Both California and federal law allow members of the clergy an exclusion from income for either the rental value of a home furnished is part of their compensation or for a rental allowance paid as part of their compensation to the extent it is used to provide a home. Effective 1/1/02, under federal law, the exclusion for the rental allowance is limited to the fair rental value of the home (including furnishings and a garage) and the cost of utilities. California does not limit the exclusion for the rental allowance to the fair rental value of the home.	Enter on Schedule CA (540 or 540NR), line 7, column B the excess housing allowance exclusion allowed for California over the federal exclusion.
Housing exclusion for state-employed clergy	Effective 1/1/03, for clergy members employed by the State of California, up to 50% of gross salary may be allocated for either the rental value of a home furnished or the rental allowance paid to them to rent or provide a home.	If the amount of your federal exclusion is less than your California exclusion, enter the adjustment on Schedule CA (540 or 540NR), line 7, column B. If the amount of your federal exclusion is greater than your California exclusion, enter the adjustment on Schedule CA (540 or 540NR), line 7, column C.
Employer-provided adoption assistance exclusion	Both federal and California law provide for an exclusion of adoption expenses paid or incurred by an employer on behalf of an employee pursuant to an adoption assistance program. For 2003, federal law limits the exclusion of expenses to \$10,160 for the aggregate of the expenses paid or incurred by the employer for the year the adoption becomes final and for all prior years. In the case of an adoption of a child with special needs, federal law provides for a potential increase in the exclusion for the year in which the adoption becomes final above actual expenses paid or incurred by the employer. The increase is the excess (if any) of \$10,160 over the aggregate of all current year and all prior year adoption expenses. With regard to adoptions of children with special needs, California does not conform to the federal provisions providing for a potential increase in the exclusion for the year in which the adoption becomes final or the limitation based upon the aggregate amount paid in all years.	Get form FTB 5123, Employer-Provided Adoption Assistance Exclusion, to calculate the California exclusion. If the amount of your federal exclusion is less than your California exclusion, enter the adjustment on Schedule CA (540 or 540NR), line 7, column B. If the amount of your federal exclusion is greater than your California exclusion, enter the adjustment on Schedule CA (540 or 540NR), line 7, column C.

Taxable Interest Income

- Non-California bonds: - United States - Other states - Loans made to a business located in an enterprise zone	Federal law requires the interest earned on federal bonds (U.S. obligations) to be included in gross income. California does not tax this interest income. The following are not considered U.S. obligations for California purposes: Federal National Mortgage Association (Fannie Mae); Government National Mortgage Association (Ginnie Mae); or Federal Home Loan Mortgage Corporation (Freddie Mac). Federal law does not tax interest from state or local bonds. California taxes the interest from non-California state and local bonds. California law allows a deduction from income for the amount of net interest received from loans made to a trade or business located within an enterprise zone. Federal law has no comparable deduction.	Enter the amount of federal bond interest included in federal income on Schedule CA (540 or 540NR), line 8, column B. Enter the interest from non-California state or local bonds on Schedule CA (540 or 540NR), line 8, column C. Use form FTB 3805Z, Enterprise Zone Deduction and Credit Summary. Transfer the net interest deduction from form FTB 3805Z to Schedule CA (540 or 540NR), line 8, column B. Write "FTB 3805Z" next to the dotted line on Form 540 or Long Form 540NR, line 14.
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ITEM	DIFFERENCES BETWEEN FEDERAL AND CALIFORNIA LAW	WHAT TO DO FOR CALIFORNIA
Interest income received in conjunction with the refund of the smog impact fee	California law provides an income exclusion for interest received from the State of California in conjunction with the refund of the smog impact fee for individuals who were not allowed to deduct the smog impact fee when it was paid.	Enter the interest on Schedule CA (540 or 540NR), line 8, column B.
Dividend Income		
Exempt interest dividends (Mutual Funds)	California taxes dividends derived from mutual funds that are paid from interest received from obligations (bonds) issued by non-California states or municipalities in other states. California does not tax dividends paid by a fund attributable to interest received from U.S. obligations or California state or municipal obligations IF at least 50% of the fund's assets would be exempt from California tax when held by an individual. The fund will provide a statement regarding the dividends it pays.	If the value of U.S. and California state or municipal obligations is at least 50% of the fund's total assets, enter the amount of exempt interest dividends that are attributed to U.S. obligations that are included in federal income on Schedule CA (540 or 540NR), line 9, column B. If the taxpayer received any dividends from the fund attributable to obligations issued by non-California states or municipalities within other states that were excluded from the taxpayer's federal income, enter that excluded amount on Schedule CA (540 or 540NR), line 9, column C.
Controlled foreign corporation (CFC)	California taxes CFC dividends in the year distributed rather than in the year earned.	If CFC dividends are earned in one year and distributed in a later year, enter the dividends included in federal income for the year earned on Schedule CA (540 or 540NR), line 9, column B and enter the dividends for the year distributed on Schedule CA (540 or 540NR), line 9, column C.
Regulated investment company (RIC)	California taxes the undistributed capital gain from a RIC in the year distributed rather than in the year earned.	If capital gain from a RIC is earned in one year and distributed in a later year, enter the capital gain included in federal income for the year earned on Schedule CA (540 or 540NR), line 9, column B and enter the capital gain for the year distributed on Schedule CA (540 or 540NR), line 9, column C.
Distributions of pre-1987 earnings from S corporations	Prior to 1987, California treated all federal S corporations as C corporations. So when a federal S corporation first becomes a California S corporation, its initial accumulated adjustments account (AAA) has a zero balance regardless of the federal AAA balance. If distributions from the S corporation exceed the California balance in the AAA, you have a distribution from pre-1987 earnings.	Enter distributions from pre-1987 earnings (or earnings in any later year that the corporation was a federal S corporation and a California C corporation) on Schedule CA (540 or 540NR), line 9, column C.
Noncash patronage dividend from farmers' cooperatives or mutual associations	Federal law taxes the dividend in the year of receipt. California permits an election to include the dividend in gross income either when received or when redeemed. Once an election is made, this method must be followed unless a change in the method of reporting is approved by the Franchise Tax Board (FTB).	If you elect or elected to include the dividend in the year redeemed, enter the amount received in 2003 on Schedule CA (540 or 540NR), line 9, column B. Enter the amount redeemed in 2003 on Schedule CA (540 or 540NR), line 9, column C.
Taxable Refunds, Credits, or Offsets of Local Income Taxes		
State income tax refund	Federal law includes the state income tax refund in income. California excludes the state income tax refund from income.	Enter the amount of state income tax refund included in federal income on Schedule CA (540 or 540NR), line 10, column B.
Alimony Paid		
Alimony paid by a nonresident alien	Alimony expense paid by a nonresident alien that was not deducted on the federal return is a deduction on the California return.	Enter the amount not included on your federal return on Schedule CA (540 or 540NR), line 32a, column C.
Alimony Received		
Alimony received by a nonresident alien	Alimony received which was not included on the federal return must be included on the California return.	Enter the amount not included in federal income on Schedule CA (540 or 540NR), line 11, column C.

ITEM	DIFFERENCES BETWEEN FEDERAL AND CALIFORNIA LAW	WHAT TO DO FOR CALIFORNIA
Business Income or (Loss) — Depreciation, Amortization, and Property Expensing		
Income from a business, trade, or profession conducted partially in California	If a nonresident owns a business, trade, or profession carried on within California that is an integral part of a unitary business carried on both within and outside California, the amount of such income having its source in California is determined in accordance with the provisions of R&TC Sections 25120 through 25141.	Gross income from the entire business, trade, or profession is included in the nonresident's adjusted gross income from all sources. The nonresident's California source business income is generally determined by a 4-factor apportionment formula (property, payroll, and sales). Refer to Cal. Code Regs., tit. 18, section 17951.
Asset expense election (IRC Section 179)	Federal law allows an expense election up to \$100,000 of the cost of certain business property in lieu of depreciation. California allows an expense election up to \$25,000. The federal Section 179 property cost phaseout starts at \$400,000. The California phaseout starts at \$200,000. Federal law allows a Section 179 expense election for off-the-shelf software; California does not conform.	Use form FTB 3885A to figure the necessary adjustment to make on Schedule CA (540 or 540NR).
MACRS recovery period for nonresidential real property	For federal purposes, the recovery period for nonresidential real property is 39 years. California conformed to this provision on 1/1/97. The California recovery period of 31.5 years should be used for property placed in service on or after 5/13/93, and before 1/1/97.	Use form FTB 3885A to figure the depreciation adjustment to make on Schedule CA (540 or 540NR).
Depreciation of assets acquired prior to 1/1/87	Federal law allowed the rapid write-off of tangible personal property and buildings over recovery periods which were shorter than economic useful lives under the Accelerated Cost Recovery System (ACRS). California law in general was not conformed to federal law but did allow ACRS for certain residential rental property constructed in California on or after 7/1/85, and before 1/1/87.	Use form FTB 3885A to figure the adjustment to make on Schedule CA (540 or 540NR).
Depreciation	Federal law allows an additional 30% first-year depreciation deduction and AMT depreciation adjustment for property placed in service after 9/10/01. The first-year depreciation deduction is increased to 50% for property placed in service after 5/5/03. California has not conformed to these provisions.	Use form FTB 3885A to figure the adjustment to make on Schedule CA (540 or 540NR).
Amortization of goodwill and certain other intangibles	Property classified as IRC Section 197 property under federal law is also Section 197 property for California purposes. However, for Section 197 property acquired before 1/1/94, the California basis as of 1/1/94, must be amortized over the remaining federal amortization period.	Use form FTB 3885A to figure the adjustment to make on Schedule CA (540 or 540NR).
Business property moves into California	Depreciation methods and useful lives of trade or business property must be acceptable to California.	If an unacceptable method was used before the move into California, use the straight-line method to compute the basis in the property.
Enterprise Zone, Local Agency Military Base Recovery Area (LAMBRA), or Targeted Tax Area (TTA) business expense deduction	Federal law has no comparable deduction. A California enterprise zone business may elect to immediately expense up to \$40,000 of the cost of qualified property. A California LAMBRA business may elect to immediately expense up to \$40,000 of the cost of qualified property. A California TTA business may elect to immediately expense up to \$40,000 of the cost of qualified property. For California purposes, you may not take an IRC Section 179 deduction on any asset used to calculate the business expense deduction.	Use form FTB 3805Z, form FTB 3807, or form FTB 3809. Enter the business expense deduction from form FTB 3805Z, form FTB 3807, or form FTB 3809 on Schedule CA (540 or 540NR), line 12, line 17, or line 18, column B. Use form FTB 3885A to figure any depreciation adjustment to make on Schedule CA (540 or 540NR).
Accelerated depreciation for property on Indian reservations	Under federal law, certain property on Indian reservations placed in service after 1/1/94, and before 1/1/05, will be subject to special MACRS recovery periods. California did not conform to this provision. See federal Publication 3991.	Use form FTB 3885A to figure the depreciation adjustment to make on Schedule CA (540 or 540NR).
Pollution control facilities	Both California and federal law provide for accelerated write-off of pollution control facilities. California law only allows the write-off of facilities located in California.	Enter the amortization for the California facilities on form FTB 3885A. Compare the California amortization to the federal amortization and enter the difference on Schedule CA (540 or 540NR), line 12 or line 17, column C.

ITEM	DIFFERENCES BETWEEN FEDERAL AND CALIFORNIA LAW	WHAT TO DO FOR CALIFORNIA
Expenditure for tertiary injectants incurred in the crude oil industry	Federal law allows a deduction for the cost of tertiary injectants which are part of a tertiary recovery system. California law allows a depreciation deduction if the tertiary injectant qualifies as property used in a trade or business or is held for the production of income.	Enter the amount of tertiary injectants deducted on your federal return on Schedule CA (540 or 540NR), line 12, column C. Attach a schedule reflecting the depreciation computation of tertiary injectants placed in service during 2003. Then complete form FTB 3885A.
Reduced recovery periods for fruit bearing grapevines replaced in a California vineyard on or after 1/1/92, as a result of phylloxera infestation on or after 1/1/97, as a result of Pierce's disease	Federal law generally requires a 10-year recovery period for fruit bearing vines for purposes of accelerated cost recovery and a 20-year recovery period for those vines under an alternative depreciation system. California law allows 5 and 10-year recovery periods, respectively.	Prepare a schedule reflecting the depreciation computation of grapevines placed in service on or after 1/1/92 (for phylloxera infestation), and placed in service on or after 1/1/97 (for Pierce's disease). Then complete form FTB 3885A and attach it and your depreciation schedule to your return.
Income forecast method of depreciation	For assets placed in service after 8/5/97, federal law limits the income forecast method of depreciation to film, video tape, sound recordings, copyrights, books, patents, and other property to be specified by federal regulations. California conformed to this limitation for assets placed in service after 12/31/97.	Use form FTB 3885A to figure the depreciation adjustment to enter on Schedule CA (540 or 540NR).
Clean fuel and electric vehicles classified as luxury automobiles	For electric vehicles and automobiles equipped to qualify as clean-burning fuel vehicles placed in service after 8/5/97, and before 1/1/05, federal law allows a modified depreciation limitation equivalent to triple the IRC Section 280F limitation for other luxury automobiles. California conformed to this provision for assets placed in service after 12/31/97.	Use form FTB 3885A to figure the depreciation adjustment to enter on Schedule CA (540 or 540NR).
Business Income or (Loss) — Adjustments to Basis or Business Deductions		
Donated agricultural products transportation credit	Federal law has no comparable credit. Under California law, deductions are not allowed for the portion of expenses equal to the credit.	Enter on Schedule CA (540 or 540NR), line 12, line 17, or line 18, column C, the portion of the deduction claimed on your federal return that was used to claim the California credit.
Farmworker housing credit	Federal law has no comparable credit. Under California law, deductions are not allowed for the portion of expenses equal to the credit.	Enter on Schedule CA (540 or 540NR), line 12, line 17, or line 18, column C, the portion of the deduction claimed on your federal return that was used to claim the California credit.
Rice straw credit	Federal law has no comparable credit. Under California law, deductions are not allowed for the portion of expenses equal to the credit.	Enter on Schedule CA (540 or 540NR), line 12, line 17, or line 18, column C, the portion of the deduction claimed on your federal return that was used to claim the California credit.
Clean fuel vehicles first year deduction	California has not conformed with federal law for the first year deduction on Clean Air Fuel.	Add the amount deducted from federal income to the total on Schedule CA (540 or 540NR), line 33, column B.
Basis adjustment for sales or use tax credit for property used in an Enterprise Zone, a LAMBRA, the Targeted Tax Area (TTA), or the former LARZ.	Federal law has no comparable credit, but IRC Section 164(a) requires an increase in basis for the amount of sales or use tax paid. Under California law, depreciation is computed based on cost, without regard to the sales or use tax allowed as a credit. Federal and state basis will differ due to the increase in federal basis by the addition of the sales or use tax.	Use form FTB 3805Z, form FTB 3807, form FTB 3809, or form FTB 3806 to claim the sales or use tax credit for property used in an Enterprise Zone, a LAMBRA, the TTA, or the former LARZ. Complete form FTB 3885A, Part III if you are depreciating the cost of the property in excess of the allowable credit.
Credit for employer-paid child care center and services	Federal law allows a deduction for all ordinary and necessary trade or business expenses. Under California law, employers may claim a credit of 30% of the costs for establishing a child care program or contributing to a child care referral service. Deductions are not allowed for that portion of expenses equal to the credit. Reduce the basis of any child care facility by the amount of the credit attributable to the facility in the year the credit is allowed.	Enter 30% of the amount of deductions claimed on your federal return to operate a child care program or contribute to the referral service on Schedule CA (540 or 540NR), line 12, column C. Then complete form FTB 3885A.

ITEM	DIFFERENCES BETWEEN FEDERAL AND CALIFORNIA LAW	WHAT TO DO FOR CALIFORNIA
Credit for employer-paid child care plan	Federal law allows a deduction for all ordinary and necessary trade or business expenses. Under California law, employers and building owners may claim a credit of 30% of contributions to a qualified care plan on behalf of any dependent under the age of 12 of the employer's California employee. Deductions are not allowed for that portion of the expenses equal to the amount of the credit. If the contribution to the plan is used at a facility owned by the employer, the basis of the facility must be reduced by the amount of the credit attributable to the facility in the year the credit is allowed.	Enter 30% of the amount of deductions claimed on your federal return for costs paid for contributions to a qualified care plan made on behalf of a California employee's dependent(s) under the age of 12 on Schedule CA (540 or 540NR), line 12, column C. Then complete form FTB 3885A.
Enhanced oil recovery credit	Federal law allows a credit for up to 15% of qualified costs attributable to qualified enhanced recovery oil projects. The basis of the enhanced recovery oil projects must be reduced by the amount of the credit. California conforms to this provision, except that only California projects qualify for the state credit, and the amount of the credit is limited to 1/3 of the federal credit amount.	Get form FTB 3546, Enhanced Oil Recovery Credit.
Solar or wind energy system credit	California law allows taxpayers to claim a credit for the purchase and installation of a solar or wind energy system. The credit is the lesser of 15% of the costs and installation of a solar or wind energy system or \$4.50 per rated watt of generating capacity of the system.	Get form FTB 3508, Solar Energy System Credit.
Joint Strike Fighter wage credit/Joint Strike Fighter property credit	California allows a credit for 30% of qualified wages paid or incurred, not to exceed \$10,000 for each qualified employee, or a proportional amount for an employee who is employed by the taxpayer for only part of the taxable year for duties related to a joint strike fighter. Federal law has no comparable credit. California allows a credit for 10% of the cost of property placed in service in California for ultimate use in a joint strike fighter. Federal law has no similar credit.	Get form FTB 3534, Joint Strike Fighter Credit.
Disabled access credit for eligible small businesses	Federal law allows a credit of 50% for the cost of making a business accessible to disabled individuals. No deduction is permitted for any amount for which a disabled access credit is allowed. California conforms to this provision, but the maximum credit is \$125 (50% of eligible expenses up to \$250).	Get form FTB 3548, Disabled Access Credit for Eligible Small Businesses.
Indian employment credit	Under federal law, a nonrefundable credit is available to employers for certain wages and health insurance costs paid or incurred by the employer after 1/1/94, for certain full-time or part-time employees who also are enrolled members of an Indian tribe or are spouses of enrolled members. California did not conform to this provision.	Enter the amount of business expense denied under federal law on Schedule CA (540 or 540NR), line 12, line 17, or line 18, column B.
Abandonment or tax recoupment fees for open-space easements and timberland preserves	Federal law allows a deduction for expenses incurred in a trade or business or for the production of income. California denies a deduction for fees paid by California property owners on termination of open-space easements or timberland preserve status.	Enter the amount of fees incurred and deducted on your federal return on Schedule CA (540 or 540NR), line 12, line 17, or line 18, column C.
Enterprise Zone, LAMBRA, or Manufacturing Enhancement Area (MEA) hiring credit	Under California law, employers may claim a hiring credit related to an Enterprise Zone, a LAMBRA, or an MEA. Deductions for the wages upon which the credit is based must be reduced by the amount of credit.	Enter the amount of wages (from form FTB 3805Z, form FTB 3807, or form FTB 3808) equal to the amount of your California credit on Schedule CA (540 or 540NR), line 12, line 17, or line 18, column C.
Real Estate Professionals – Material participation in a rental real estate activity	Beginning with the 1994 tax year 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 and these activities are still considered passive under California law.	To figure the adjustment to make on Schedule CA (540 or 540NR), line 17, use form FTB 3801, Passive Activity Loss Limitations, and include these activities when completing the California Passive Activity Worksheet and the California Adjustment Worksheets in the instructions for form FTB 3801.

ITEM	DIFFERENCES BETWEEN FEDERAL AND CALIFORNIA LAW	WHAT TO DO FOR CALIFORNIA
Research credit	Federal law allows a credit for research expenses and requires that the deduction for research expenses be reduced by the amount of the credit allowed. California conforms to federal law, but requires the amount of research expenses to be reduced by the amount of the California credit. In addition, California law requires the use of the California tax bracket when determining the elective credit amount.	Enter the amount of research expenses deducted on your federal return on Schedule CA (540 or 540NR), line 12, line 17, or line 18, column C. Enter the amount of California research expenses after reduction for California research credit on Schedule CA (540 or 540NR), line 12, line 17, or line 18, column B.
Property for which a public utility provided an energy conservation subsidy on or after 1/1/95, and before 1/1/97	Federal law allows an exclusion from income for any subsidy provided directly or indirectly by a public utility for the purchase or installation of any energy conservation measure with respect to a dwelling unit. The adjusted basis of the property must be reduced by the amount excluded from income. California does not conform for amounts received after 12/31/94, and before 1/1/97.	Use form FTB 3885A to figure the adjustment to enter on Schedule CA (540 or 540NR).
Employer wage expenses for Work Opportunity Credit and Welfare-To-Work Credit	Federal law allows a Work Opportunity Credit and a Welfare-To-Work Credit for employers that hire individuals from certain target groups and recipients of long-term family assistance. Employers that claim these credits must reduce their wage expense by the amount of the credits. California has no similar credits.	Enter the amount of the federal Work Opportunity Credit or Welfare-To-Work Credit that reduced the federal deduction for wages on Schedule CA (540 or 540NR), line 12, line 17, or line 18, column B.
Qualified clinical testing expenses	Federal law allows an Orphan Drug Credit for qualified clinical testing expenses incurred in testing drugs for rare diseases or conditions. A business must reduce its deduction for qualified clinical testing expenses by the amount of the credit. California has no similar credit.	Enter the amount of the federal Orphan Drug Credit that reduced the federal deduction for qualified clinical testing expenses on Schedule CA (540 or 540NR), line 12, line 17, or line 18, column B.
Business expense	California does not allow a deduction for business expenses incurred at a club that discriminates.	Enter on Schedule CA (540 or 540NR) line 12, column C, the amount taken as a federal deduction.
Qualified environmental cleanup costs	Federal law allows an election to currently deduct costs paid or incurred on or after 8/5/97, for cleanup costs at a qualified contaminated site. California did not conform to this provision until 1/1/98. Therefore, before 1/1/98, such costs were classified as capital expenditures for California purposes.	Use form FTB 3885A to figure the adjustment to enter on Schedule CA (540 or 540NR).
Capital Gains and Losses		
Gain on sale or disposition of a qualified assisted housing development to low-income residents or to specified entities who maintain housing for low-income residents	Federal law does not allow special treatment on gains related to the sale of certain assisted housing. California law permits the deferral of such gain, under certain conditions, if the proceeds are reinvested in residential real property (other than a personal residence) within two years of the sale.	Enter the transaction on California Schedule D (540 or 540NR), line 1. In column (e) enter "-0- R&TC Section 18041.5." Reduce the basis of replacement property by the gain deferred. Attach a schedule to your return reflecting computation of basis in the replacement property, or a statement of intent to replace within the replacement period.
Gain on sale of personal residence	For sale or exchanges after 5/6/97, federal law allows an exclusion of gain on the sale of a personal residence in the amount of \$250,000 (\$500,000 if married filing jointly). The taxpayer must have owned and occupied the residence as a principal residence for at least 2 of the 5 years before the sale. California conforms to this provision. However, taxpayers who served in the Peace Corps during the 5 year period ending on the date of the sale may reduce the 2 year period by the period of service, not to exceed 18 months.	Report gain on the sale of a personal residence on California Schedule D (540 or 540NR), line 1, column (e). Cost or other basis plus expense of sale must reflect adjustment for depreciation allowed or allowable for California purposes.

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Military and U.S. Foreign Service member's suspension of five-year test period for exclusion of gain on the sale of personal residence	Both federal and California law allow an exclusion of \$250,000 (\$500,000 for married filing jointly) of capital gain realized from the sale of a principal residence. Generally the taxpayer must own the home and use it as a personal residence for two of the last five years ending on the date of the sale. For federal purposes, military and U.S. Foreign Service personnel on qualified official extended duty can elect a suspension, for up to ten years, of the five-year test period for ownership and use of a principal residence for the purpose of qualifying for the exclusion. Federal law allows the suspension for qualified official extended duty to be applied retroactively to sales on or after 5/7/97. Qualified official extended duty is duty at least 50 miles from the individual's principal residence or when orders compel residence in government furnished quarters. The duty must be for more than 90 days or for an indefinite period. California does not conform to the suspension of the five-year test period.	Enter on Schedule CA (540 or 540NR), line 13, column C, the gain excluded under federal law as a result of the election to suspend the five-year test period that otherwise would not qualify for exclusion under the normal five-year test period.
Undistributed capital gains for regulated investment company (RIC) shareholders	Federal law requires certain undistributed capital gains reported on federal Form 2439 to be included in the gross income of the mutual fund shareholder and allows a tax credit for the capital gains tax paid by the RIC. California has no similar provision.	Do not enter the amount of undistributed capital gains on California Schedule D (540 or 540NR).
Gain or loss on sale of property inherited before 1/1/87	Federal gain or loss may differ from the California gain or loss due to differences in the basis of property. For more information, get FTB Pub. 1039, Basis of Property-Decedent and Surviving Spouse. For property inherited on or after 1/1/87, the California basis and the federal basis are the same.	Report the amount of California capital gains and losses on California Schedule D (540 or 540NR).
Capital loss carrybacks	Federal law allows a deduction for carrybacks of certain capital losses. California has no similar provision.	Report the amount of California capital gains and losses on California Schedule D (540 or 540NR).
Exclusion of gain on the sale of qualified small business stock	Federal law allows an exclusion under IRC Section 1202 of 50% of the gain on the sale of qualifying small business stock originally issued after 8/10/93, that was held for more than five years. California law provides a similar exclusion (under R&TC Section 18152.5); 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 issuing corporation's assets must be used by the corporation to actively conduct one or more qualified trades or businesses in California.	Use California Schedule D (540 or 540NR) if you claim the federal IRC Section 1202 exclusion on your federal return.
Other Gains or Losses		
Basis differences of business property	The California basis of assets may be different than the federal basis due to differences between California and federal law, which may affect the gain or loss on disposition.	Get Schedule D-1, Sales of Business Property, to figure the adjustment to make on Schedule CA (540 or 540NR).
IRA Distribution		
IRA basis adjustments	There may be differences in the taxable amount of the distribution depending on when the contributions were made, if you changed residency status after you first began making contributions to your IRA or made different deductions for California because of differences between your California and federal self-employment income. You will need to calculate your IRA basis as if you were a California resident for all prior years.	Get FTB Pub. 1005, Pension and Annuity Guidelines, for more information.
Roth IRAs	Federal law and California law are the same regarding contributions, conversions, and distributions. However, the taxable amount of a distribution may not be the same because of basis differences.	Get FTB Pub. 1005, Pension and Annuity Guidelines, for more information.

ITEM	DIFFERENCES BETWEEN FEDERAL AND CALIFORNIA LAW	WHAT TO DO FOR CALIFORNIA
Pensions and Annuities		
Railroad retirement benefits	California does not tax railroad retirement benefits reported on federal Form RRB 1099-R or RRB 1099.	Enter on Schedule CA (540 or 540NR), line 16, column B, the amount of tier 1 (non-Social Security equivalent) or tier 2 railroad retirement benefits included in adjusted gross income on your federal return. Get FTB Pub. 1005, Pension and Annuity Guidelines, for more information.
Pension plan – small business tax credit for new retirement plan expenses	Federal law allows an income tax credit for 50% of the first \$1,000 in administrative and retirement-education expenses for any small business that adopts a new qualified defined benefit or defined contribution plan. The federal deduction is reduced by the amount of the credit. California has no similar credit.	Enter the amount of the income tax credit on Schedule CA (540 or 540NR), line 16, column B.
Employer-sponsored pensions and annuities (for annuity starting dates after 7/1/86, and before 1/1/87) if you elected to use the “three-year rule” for California	Under federal law, no “three-year rule” is allowed for any individual whose annuity starting date is after 7/1/86. Under California law, an individual whose annuity starting date was after 7/1/86, and before 1/1/87, could elect to use the “three-year rule” if: 1) The employer paid part of the cost and 2) During the three years from the date of the first annuity payment, the total amount receivable will equal or exceed the cost (investment) in the contract.	If your annuity starting date was after 7/1/86, and before 1/1/87, AND you elected to use the three-year recovery rule for California, an adjustment is required. Enter the difference on Schedule CA (540 or 540NR), line 16, column C. Get FTB Pub. 1005, Pension and Annuity Guidelines, for more information.
Canadian Registered Retirement Savings Plans (RRSP)	Under both federal and California law, the RRSP does not qualify as an Individual Retirement Account (IRA) and does not receive IRA treatment. The federal treaty that allows taxpayers to elect to defer taxation on their RRSP earnings until the time of distribution does not apply for California income tax purposes. California residents must include their RRSP earnings in their taxable income in the year earned.	Enter on Schedule CA (540 or 540NR), line 8, line 9, or line 13, column C, the earnings from the RRSP.
Unemployment Compensation		
Unemployment compensation	California does not tax unemployment compensation.	Enter on Schedule CA (540 or 540NR), line 19, column B, the amount of unemployment compensation you included in adjusted gross income on your federal return.
Social Security Benefits		
Social security benefits and equivalent tier 1 railroad retirement benefits	California does not tax social security benefits and equivalent tier 1 railroad retirement benefits.	Enter on Schedule CA (540 or 540NR), line 20, column B, the amount of social security benefits and equivalent tier 1 railroad retirement benefits you included in adjusted gross income on your federal return.
Rents, Royalties, Partnerships, Estates, Trusts, etc.		
Pass-through of income and deductions from partnerships, S corporations, estates, and trusts	Items of income and deduction from pass-through entities may differ due to various differences between federal and state law. Refer to federal Schedule K-1 (1065), or Schedule Q in the case of REMICs, to determine items of income and deduction for federal purposes. Refer to California Schedules K-1 (100S, 541, 565, or 568) to determine items of income and deduction from pass-through entities for California purposes.	Follow the instructions for Schedules K-1 (100S, 541, 565, or 568). Some items are reported directly on Schedule CA (540 or 540NR), line 17, and some items must be reported on other forms and schedules. Note: Part-year residents must allocate income between the period of residency and the period of non-residency in a manner that reflects the actual date of realization of partnership, S-corporation and certain trust income. In the absence of information that reflects the actual date of realization, the taxpayer must allocate an annual amount on a proportional basis between the two periods, using a daily pro rata methodology. Get FTB Pub. 1100, Taxation of Nonresidents and Individuals Who Change Residency, for more information.

ITEM	DIFFERENCES BETWEEN FEDERAL AND CALIFORNIA LAW	WHAT TO DO FOR CALIFORNIA
Accumulation distribution to beneficiaries on which the required California taxes have not been paid by a trust	Federal law taxes the accumulated income of a trust under IRC Sections 665-668. If a trust has a California resident trustee or beneficiary, the beneficiary is non-contingent, and the trust has not filed a California return and paid California tax as the income was accumulated, then the full amount of the accumulation distribution is taxable to the beneficiary in the year the accumulation distribution is received.	If you received a federal Schedule J (1041) and did not receive a California Schedule J (541), an adjustment is required because the trust did not file a California return and pay the tax as the income was accumulated. The accumulation distribution from federal Schedule J (1041) must be adjusted for California purposes. This information must be provided by the trustee.
Accumulation distribution to beneficiaries on which the trust was not required to pay California tax because the beneficiaries' interest was contingent	Federal law taxes the accumulated income of a trust under IRC Sections 665-668. If a trust has a California resident trustee or beneficiary, the beneficiary is contingent, and the trust has not filed a California return and paid California tax as the income was accumulated, then the beneficiary is entitled to the benefit of income averaging under the provisions of R&TC Sections 17745(b) and (d).	Use California form FTB 5870A, Tax on Accumulation Distribution of Trusts, to compute the part of the accumulation distribution includable in your 2003 California adjusted gross income.
Amounts included in gross income of United States shareholders from foreign corporations	Under federal law, IRC Section 951, if a foreign corporation is a controlled foreign corporation (CFC) for an uninterrupted period of 30 days or more during any taxable year, then U.S. shareholders who own stock in a CFC on the last day of the taxable year in which it was a CFC must include in gross income their pro-rata share of income. The pro-rata shares are included in the income of U.S. shareholders even though there may be intervening entities in a chain between a CFC and such shareholders. California has no similar provision.	Enter the amount of income received from a CFC and included in federal income on Schedule CA (540 or 540NR), line 17, column B.
Other Income/Adjustments to Income		
- Net Operating Loss (NOL) - Disaster loss carryover - Federal NOL deduction - California NOL deduction - NOL deduction from Enterprise Zones, LAMBRAs, the TTA, the former LARZ, or Pierce's disease - Original issue discount (OID) for debt instruments issued (and loans made) in 1985 and 1986	The allowable disaster loss carryover under California law is different than the allowable disaster loss carryover under federal law. Due to differences between federal and California law, you must refigure your NOL carryover for California purposes. The NOL deduction has been suspended for 2002 and 2003. The NOL deduction has been suspended for 2002 and 2003. In the tax year in which the debt instrument matures, is sold, exchanged, or otherwise disposed of, you must recognize the difference between the amount reported on your federal return and the amount reported for California purposes.	Enter as a positive number on Schedule CA (540 or 540NR), line 21b, column B, from your 2002 form FTB 3805V. Enter as a positive number on Schedule CA (540 or 540NR), line 21c, column C, the federal NOL deduction. Use form FTB 3805V to figure the California NOL carryover. Suspended for 2002 and 2003. Suspended for 2002 and 2003.
Income exempted by U.S. tax treaties	California is not affected by U.S. treaties with foreign countries unless they specifically apply to state income taxes. If a treaty does not specifically exempt income from state income tax, California requires the reporting of adjusted gross income from all sources.	Issuer (debtor) – Enter the difference between the federal deductible amount and the California deductible amount on Schedule CA (540 or 540NR), line 21f, column B. Holder (lender) – Enter the difference between the amount included in federal gross income and the amount included for California purposes on Schedule CA (540 or 540NR), line 21f, column C. Adjust federal income to reflect worldwide income computed under California statutes. Enter losses from foreign sources on Schedule CA (540 or 540NR), line 21f, column B. Enter foreign source income on Schedule CA (540 or 540NR), line 21f, column C.

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Foreign income of nonresident aliens	Federal Form 1040NR, U.S. Nonresident Alien Income Tax Return, and federal Form 1040NR-EZ, U.S. Income Tax Return for Certain Nonresident Aliens With No Dependents, requires that only United States source income be reported. California requires the reporting of adjusted gross income from all sources.	Adjust federal income to reflect worldwide income computed under California statutes. Enter losses from foreign sources on Schedule CA (540 or 540NR), line 21f, column B. Enter foreign source income on Schedule CA (540 or 540NR), line 21f, column C.
California lottery winnings	California does not tax California lottery winnings. California does tax lottery winnings from other states.	Enter on Schedule CA (540 or 540NR), line 21a, column B, the amount of California lottery winnings included in adjusted gross income on your federal return.
Reward from a crime hotline	California does not tax a reward authorized by a government agency and received from a crime hotline established by a government agency or nonprofit organization.	Enter on Schedule CA (540 or 540NR), line 21f, column B, the amount of such a reward you included in adjusted gross income on your federal return.
Income received from a recycling center or location for empty beverage containers	Federal law taxes beverage container recycling income. California law does not tax income received by a consumer for recycling empty beverage containers.	Enter the amount of beverage container recycling income reported on your federal return on Schedule CA (540 or 540NR), line 21f, column B.
Foreign-earned income and housing expense exclusion	Under federal law, IRC Section 911, a qualified individual may elect to exclude certain foreign-earned income and an employer-provided housing allowance. California has no similar provision.	Enter the amount of foreign-earned income and housing allowance excluded under IRC Section 911 on Schedule CA (540 or 540NR), line 21f, column C.
Educator expense	Federal law allows a deduction for qualified expenses for teachers, instructors, counselors, principals, or aides for K-12 grades. California has not conformed.	Enter the amount on Schedule CA (540 or 540NR), line 23, column B.
Student loan interest	Federal law allows a deduction for student loan interest and has eliminated the 60-month limitation. However, California will allow only the interest required to be paid on student loans for the first 60 months. California also has a different phaseout of the deduction.	Enter on Schedule CA (540 or 540NR), line 25, column B, the amount of the federal deduction not allowed for California. Use the worksheet included with the Schedule CA (540 or 540NR), line 25 instructions to calculate the California adjustment.
Tuition and fees deduction	Federal law allows a deduction from income up to \$3,000 for qualified higher education expenses paid. California has not conformed.	Enter the amount on Schedule CA (540 or 540NR), line 26, column B.
American Indians per capita payments	Federal law taxes per capita distributions regardless of where the tribal member resides. California does not tax per capita distributions received by tribal members who live in Indian country affiliated with their tribe that are sourced from the same Indian country where they are a member. California does not tax per capita distributions received by a nonresident. California taxes per capita distributions received by California resident tribal members who reside outside their affiliated tribal Indian country. Get FTB 674, Frequently Asked Questions About the Income Taxation of American Indians, for more information.	Enter on Schedule CA (540 or 540NR), line 21f, column B the per capita distributions included in federal income that are exempt for California.
Grants paid to low-income individuals	California law allows an income exclusion for grants paid to low-income individuals to construct or retrofit buildings to be more energy efficient. Federal law has no similar exclusion.	Enter the amount included in federal AGI on Schedule CA (540 or 540NR), line 21f, column B.
Rebates or vouchers from a local water agency, energy agency, or energy supplier	California law allows an income exclusion for rebates or vouchers from a local water agency, energy agency, or energy supplier for the purchase and installation of water conservation appliances and devices. Federal law has no similar exclusion.	Enter the amount included in federal AGI on Schedule CA (540 or 540NR), line 21f, column B.
Payments made for wrongful incarceration	California law allows an income exclusion for payments made due to a determination of wrongful incarceration.	Enter the amount included in federal AGI on Schedule CA (540 or 540NR), line 21f, column B.

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Foster care payments	Qualified payments to foster care providers from an agency of a state or political subdivision, or from a federally tax-exempt organization under IRC 501(c)(3), are not taxable for federal and state purposes. Beginning with the 2002 tax year and for federal purposes only, the definition of qualified payments includes payments from any qualified foster care placement agency (including for-profit agencies) licensed by a state or local government to make payments to foster care providers. California does not conform to the federal change that allows qualified payments by organizations other than a state or political subdivision or from a federally tax-exempt organization. Beginning with the 2002 tax year, federal law has no age limitation for qualified foster individuals. For California, a qualified foster individual placed by a federally tax-exempt organization under IRC 501(c)(3) must be under age 19.	Enter on Schedule CA (540 or 540NR), line 21f, column C foster care payments paid by organizations other than a state or political subdivision or from a federally tax-exempt organization. Enter on Schedule CA (540 or 540NR), line 21f, column C, foster care payments paid by an organization that is federally tax-exempt that are paid for a foster individual who is 19 years of age or older.
Military death gratuity benefit exclusion	Federal law increased the maximum military death gratuity benefit exclusion to \$12,000. The increased exclusion applies for benefits received by eligible survivors for deaths occurring on or after 9/11/01. California has not conformed to the increase in the military death gratuity benefit exclusion. California allows a \$3,000 exclusion.	Enter on Schedule CA (540 or 540NR), line 21f, column C, the difference between the federal and California exclusion.
Travel expenses of National Guard and Reserve members	For 2003, federal law allows National Guard and Reserve members a deduction for travel expenses to arrive at adjusted gross income (AGI), regardless of whether they itemize their deductions. To qualify, the travel expenses must be for National Guard or Reserve meetings over 100 miles from home and require an overnight stay. California does not conform to the deduction from gross income to arrive at AGI. For California, expenses for overnight travel to attend National Guard and Reserve meetings are deductible on Schedule A as miscellaneous itemized deductions subject to the 2% of AGI limitation.	Include on Schedule CA (540 or 540NR), line 33, column B, the expenses deducted on the federal return to arrive at AGI. Write "National Guard/Reserve travel expense" on the dotted line next to line 33. If you have a difference between California and federal itemized deductions for travel expenses, enter an adjustment on Schedule CA (540 or 540NR), line 38.
Itemized Deductions		
- Taxes - Annual tax paid by a limited partnership - Franchise tax or income taxes paid by an S corporation - State, local, and foreign income taxes paid - Other adjustments	Federal law allows a deduction for the annual tax paid by a limited partnership. California specifically disallows this deduction. Federal law allows a deduction for franchise taxes or income taxes paid under the Corporation Tax Law. California specifically disallows this deduction. California does not allow a deduction for state, local, or foreign income taxes paid, including amounts paid for State Disability Insurance (SDI) or Voluntary Plan Disability Insurance (VPDI). Adjustments to itemized deductions include: adoption related expenses, mortgage interest credit, nontaxable income expense, employee business expense, investment interest expense, gambling losses, federal estate tax, generation skipping transfer tax, prior year charitable contribution carryovers, interest on loans from utility companies, and medical benefits paid on behalf of domestic partners.	Include the amount of your federal deduction for the annual tax paid on Schedule CA (540 or 540NR), line 36. Include the amount of your federal deduction for franchise taxes paid on Schedule CA (540 or 540NR), line 36. Include the amount of your federal deduction for state, local, and foreign taxes paid on Schedule CA (540 or 540NR), line 36. See Schedule CA (540 or 540NR), line 38, for more information.