

EXAMPLE 1-3: Workin' It, LLC was formed in 2009 and generated \$250,000 in net income. Bob and Bill, the two members, who had never contributed any assets to the LLC, got in a fight and each went their separate way, taking \$125,000 each but never filing returns.

FTB sent Workin' It a demand to file the 2009–2012 returns. The FTB may hold each of the members personally liable for the tax, up to the amount they took. Bob has no assets. Bill is wealthy. The FTB can collect the entire tax liability from Bill, if he is the only one with assets to pay it.

Ralite won't work. If they file, they will at least save the \$2,000 penalty.

3. File the returns but don't pay the tax or penalties. We're not sure this buys anything except avoiding the \$2,000-per-year penalty if the FTB is able to collect from the member.

Penalty relief

R&TC §19135 contains a reasonable cause exception to the LLC \$2,000 failure-to-file penalty. We seriously doubt the FTB will consider any of the following reasonable cause:

- "I didn't know I had to file."
- "My tax professional told me I didn't have to file."
- "I don't believe I am doing business in California and therefore am not required to file."

Statute of limitations

We have also heard the incorrect theory that the statute of limitations on the old returns has expired if the income is included in the member's return. Unfortunately, this argument has no merit because the filing requirement is not for the member's individual or corporate return, but for the LLC return.



Can you guess the total 2013 federal and California tax rate?

High income taxpayers may be surprised.

By Richard B. Malamud, CPA, J.D., LL.M.
Guest Contributor

Taxes used to be easy. The federal income tax rate was 15% on dividends and long-term capital gains and 9.3% for California. California then raised the maximum rate to 12.3% and added an additional 1% for income over \$1 million, although not in that order.

Not to be outdone, the federal government raised the capital gains rate to 20%, plus added the new Medicare tax on certain incomes when AGI is over \$250,000 if married filing joint, and a surtax on net investment income. For regular income, such as salary, Congress also raised the regular maximum tax rate from 35% to 39.6%.

To find out what the real taxes are for California residents, while trying to keep it simple, the chart on page 4 represents a married couple's federal and California joint income tax and surtaxes assuming all income is either 1) salary or 2) either qualified dividends or long-term capital gains. The only itemized deduction taken into account is the resulting California tax deduction which is assumed to be paid in the year the income is earned.

The result is that for those making \$500,000 to \$10 million in wages, their federal and California income tax and Medicare surcharge will range from just under 36% to just under 49%, not counting the FICA taxes. If instead they earn all their income from long-term capital gains or qualified dividends, their total tax rate will vary from 23.4% to 36%.

What isn't calculated in these examples is the effect of the Alternative Minimum Tax. That is because the examples don't include property taxes, vehicle taxes, and miscellaneous itemized deductions, which might reduce the federal tax somewhat until those AMT adjustments kick in.

When the FICA taxes and Medicare taxes, which are withheld on wages, are added to these totals, the total taxes paid to the federal and state will exceed 50% on salary and interest income.

It should be fun trying to explain the tax increase when the 2013 completed tax returns are sent out this tax season.

2013 Wages Only Joint Return — Assumes Only CA Tax Deduction						
Wages Only	Fed Tax	AMT	Ad. 0.9%	CA Tax	CA MH	Total
			Medicare Tax			
\$ 500,000	\$ 131,826	\$ 4,584	\$ 2,250	\$ 40,898	\$ -	\$ 179,558
	26.37%	0.92%	0.45%	8.18%		35.91%
\$ 1,000,000	\$ 313,924	\$ -	\$ 6,750	\$ 96,055	\$ -	\$ 416,729
	31.39%	0.00%	0.68%	9.61%		41.67%
\$ 5,000,000	\$ 1,734,901	\$ -	\$ 42,750	\$ 587,807	\$ 39,922	\$ 2,405,380
	34.70%	0.00%	0.86%	11.76%	0.80%	48.11%
\$10,000,000	\$ 3,510,961	\$ -	\$ 87,750	\$ 1,202,807	\$ 89,922	\$ 4,891,440
	35.11%	0.00%	0.88%	12.03%	0.90%	48.91%
Long-Term Capital Gains or Qualified Dividends						
	Fed Tax	AMT	Adl. 3.8%	CA Tax	CA MH	Total
			NIIT Tax			
\$ 500,000	\$ 59,645	\$ 6,980	\$ 9,500	\$ 40,898	\$ -	\$ 117,023
	11.93%	1.40%	1.90%	8.18%		23.40%
\$ 1,000,000	\$ 151,614	\$ 15,011	\$ 28,500	\$ 96,055	\$ -	\$ 291,180
	15.16%	1.50%	2.85%	9.61%		29.12%
\$ 5,000,000	\$ 869,279	\$ 97,346	\$ 180,500	\$ 587,807	\$ 39,922	\$ 1,774,854
	17.39%	1.95%	3.61%	11.76%	0.80%	35.50%
\$10,000,000	\$ 1,761,343	\$ 205,282	\$ 370,500	\$ 1,202,807	\$ 89,922	\$ 3,629,854
	17.61%	2.05%	3.71%	12.03%	0.90%	36.30%

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