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California Tax Withholding Requirements for Rent Payments

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The California Franchise Tax Board has required withholdings in connection with real property sales for years. The FTB has now expanded withholding obligations to require withholdings on rent payments made to non-resident landlords.

The FTB initially focused on withholdings for commercial properties (by tenants and property managers). It expanded withholding obligations to residential property managers in January 2010.

Withholding is required on payments made to nonresidents of California. Nonresidents may be nonresident individuals, or corporations, LLCs or partnerships that are not qualified to do business in California. The withholding amount is seven percent (7%).

Withholdings must be submitted quarterly to the California Franchise Tax Board with a FTB Form 592, Quarterly Nonresident Withholding Statement. Before January 31st of the following calendar year, the withholding tenant or property manager must provide the landlord with a statement showing the total amount of income subject to withholding and the total amount withheld, using a FTB Form 592-B, Nonresident Withholding Tax Statement.

Withholding is not required:

- (1) For California resident landlords;
- (2) For corporations, LLCs or limited partnerships qualified to do business in California. The California Secretary of State's website at <http://kepler.sos.ca.gov> can be used to determine qualification to do business in California;
- (3) To landlords that are tax exempt organizations; banks or banking associations, insurance companies, IRAs, qualified pension and profit sharing plans, and California non-grantor trusts;
- (4) For landlords with a permanent place of business in California, unless the tenant or property manager believes that the address is merely a forwarding address (i.e. a permanent place of business must be a California street address. A California street address does not include a California post office box or an "in care of" address) and if an owner's address changes, the owner's residency and withholding obligations should be reevaluated. The California street address must be the address of the owner; if the funds are deposited rent into a California bank account for the benefit of an owner that lives out of state, withholding is required;
- (5) If the California Franchise Tax Board has issued a waiver approval letter to the landlord. Nonresident landlords may request a waiver from the California Franchise Tax Board by submitting a FTB Form 588, Nonresident Withholding Waiver Request;
- (6) If the California Franchise Tax Board has issued a Request for Reduced Withholding – Approval letter, less than 7% may be withheld. Reduced withholding may be requested by submitting a FTB Form 589 - Nonresident Reduced Withholding Request - to the Franchise Tax Board;

- (7) On the first \$1,500 in payments made during the calendar year (with the exception that there is no minimum threshold for foreign partners). Withholdings may be made on the first \$1,500, but it is not required; or
- (8) For residential property tenants (residential property managers may still be required to withhold).

To establish that the requirements of withholding exceptions 1-4 above are met, tenants or property managers may request a landlord to provide a FTB Form 590, Withholding Exemption Certificate, to establish that the landlord meets one of the exemptions. An FTB Form 590 can be requested, but is not required for exception 4, unless the withholding agent believes that the address is merely a forwarding address. Tenants or property managers can rely on a Form 590 only if they believe it is accurate and it is complete.

Withholding is required only on the payment made to the landlord, after property expenses and management fees have been deducted from the gross receipts. Withholding is not required for expense reimbursements that are separately accounted for and are not subject to 1099 reporting.

Nonresident withholding is a prepayment of California state income tax or franchise tax for nonresidents, similar to wage withholding. After the landlord files a tax return, and the withheld amount is more than the landlord's actual tax liability, the Franchise Tax Board will refund the overpayment.

A tenant or property manager who fails to furnish an accurate Form 592-B—Quarterly Resident & Nonresident Withholding Statement to a landlord may be penalized \$50 per form. If the failure is an intentional disregard for the requirement, the penalty is the greater of \$100 or 10 percent of the amount required to be reported. Penalties may also be assessed if the Form 592-B is late.

A tenant or property manager who fails to withhold, under withholds, or fails to remit withheld amounts to the FTB, may be liable for the greater of:

- the amount withheld; or
- the amount of taxes due from the landlord, but no more than the amount that should have been withheld.

In addition, the tenant or property manager may be responsible for interest and penalties.

To educate property owners about this requirement, and to reduce the chances of a dispute between the property manager and property owner regarding withholdings, property managers may wish to include a provision in management agreements authorizing withholdings unless the property owner provides proof that the property owner is not subject to the non-resident withholding requirements.

For more information see:

- A decision chart for withholding is available at www.ftb.ca.gov/individuals/wsc/decision_chart.shtml
- FTB Publication 1017, Nonresident Withholding Guidelines www.ftb.ca.gov/forms/misc/1017.pdf
- Form 588 – Nonresident Withholding Waiver Request

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- www.ftb.ca.gov/forms/misc/588.pdf
- Form 590 – Withholding Exemption Certificate www.ftb.ca.gov/forms/2016/16_590.pdf
- Form 590 – P – Nonresident Withholding Exemption Certificate for Previously Reported Income www.ftb.ca.gov/forms/2016/16_590p.pdf
- Form 592 – Quarterly Resident & Nonresident Withholding Statement www.ftb.ca.gov/forms/2016/16_592.pdf
- Form 592 – B – Resident and Nonresident Withholding Tax Statement www.ftb.ca.gov/forms/2016/16_592b.pdf
- A summary of the FTB's nonresident withholding process is available at www.ftb.ca.gov/individuals/wsc/summary_nonresident_withholding_process.shtml
- Other withholding forms and publications are available at www.ftb.ca.gov/individuals/wsc/forms_and_publications.shtml

If you have questions regarding this article, please call Jamie Sternberg at (800) 574-5587.

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