

Penalty notices resulting from mortgage debt forgiveness cancellation of debt (COD) income

PURPOSE OF BULLETIN

To tell staff that California does **not** conform to the federal Mortgage Forgiveness Debt Relief Act of 2007.

BACKGROUND

California does **not** conform to the federal Mortgage Forgiveness Debt Relief Act of 2007 that allows taxpayers to exclude the discharge of qualified principal residence indebtedness from income. For federal purposes, this applies to discharges occurring on or after January 1, 2007, and before January 1, 2010. There is pending California legislation that would generally conform to the federal changes. The pending legislative bills are:

- ☐ Senate Bill 1055
- ☐ Assembly Bill 1918
- ☐ Senate Bill 1242

Under current state law, any amount excluded under federal legislation will need to be included in California taxable income and reported as an adjustment on Schedule CA (540 or 540NR) line 21F, column C.

Individuals who did not include cancellation of debt income in the calculation of their estimated taxes may receive an estimated tax penalty.

PROCEDURES

If you receive a call from a taxpayer who has a notice for the underpayment of estimated tax penalty, and has cancellation of debt income from the discharge of qualified principal residence indebtedness, follow the steps below:

- ☐ Explain we do not conform to the federal law allowing this exclusion of COD income.
- ☐ The penalty based on the COD income is correct and must be paid.

Tell them about the pending legislation, which they can track online:

- ☐ Go to <http://leginfo.ca.gov/index.html>
- ☐ Select "Bill Information"
- ☐ Enter the bill number, click the box "Search"
- ☐ Select that bill

From there, they can check the status, history, and any amended versions.

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