

ANALYSIS OF AMENDED BILL

Franchise Tax Board

Author: Correa Analyst: Angela Raygoza Bill Number: SB 653
See Legislative
Related Bills: History Telephone: 845-7814 Amended Date: April 21, 2009, and
May 6, 2009
Attorney: Patrick Kusiak Sponsor: _____

SUBJECT: Foreign Limited Liability Companies/Federally Recognized Indian Tribes

SUMMARY

This bill would allow limited liability companies organized and operated under tribal law to qualify to do intrastate business.

SUMMARY OF AMENDMENTS

The April 21, 2009, amendments would have expanded the definition of a foreign limited liability company (LLC) to include an LLC formed under the LLC laws of any jurisdiction, other than this state or a foreign country.

The May 6, 2009, amendments would do the following:

- Expand the definition of a foreign LLC to include an LLC formed under the laws of any other state or LLCs formed under the laws of a federally recognized Indian tribe and
- Extend the tax and fee on LLCs to an LLC formed under the laws of a federally recognized Indian tribe.

This is the department's first analysis of the bill.

PURPOSE OF THE BILL

According to the author's office, the purpose of this bill is to allow federally recognized tribes to protect their assets and diversify their business ventures.

EFFECTIVE/OPERATIVE DATE

This bill would be effective and operative on and after January 1, 2010.

POSITION

Pending.

ANALYSIS

Board Position:	Department Director	Date
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<input type="checkbox"/> SA		
<input type="checkbox"/> N		
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FEDERAL/STATE LAW

Indian tribes are treated as sovereign nations under federal law, and state jurisdiction over civil and criminal matters involving tribal members or organizations is limited absent congressional authorization. States possess no power to tax Indian reservation lands or income derived from activities carried on within the boundaries of an Indian reservation.

The Beverly-Killea Limited Liability Company Act (LLC Act) first authorized the organization of LLC's in California in 1994 and also recognized LLC's organized under the laws of other states. An LLC is a hybrid form of an unincorporated business entity affording its members certain benefits, such as the following:

- Limited liability to the extent of a member's equity investment,
- Flexible management alternatives, and
- Liberal membership qualification requirements.

Members of an LLC are afforded the same advantage of limited liability as shareholders of a corporation. If an LLC is classified as a partnership for income tax purposes, the income of the LLC is generally subject to only one level of income tax, as are the partners of a partnership.

LLC's treated as partnerships for income tax purposes are not subject to the membership restrictions or the two levels of income tax imposed on S corporations.

Current federal and state law allows eligible business entities including LLC's to be treated as partnerships, corporations, or entities that are disregarded for federal tax purposes. Generally, the classification of a business entity for California purposes is required to be the same as the entity's federal classification. LLCs not classified as a corporation that are organized, registered, or doing business in California are required to pay an annual tax of \$800 and a fee measured by total income attributable to California.

For taxable years beginning on or after January 1, 2009, every limited liability company subject to the annual tax of \$800 is required to pay annually a fee based on the total income from all sources derived from or attributable to this state. The fees are as follows::

Total Gross Income of:	Fee
\$249,999 or less	- 0 -
\$250,000 - \$499,999	\$900
\$500,000 - \$999,999	\$2,500
\$1,000,000 - \$4,999,999	\$6,000
\$5,000,000 or more	\$11,790

Existing state law provides that to transact business within the state a foreign corporation, a foreign limited partnership, or a foreign LLC first register the business entity with the Secretary of State (SOS) and provide necessary information, such as the entity's agent for service of process within the state.

Existing state law defines a foreign LLC as an entity formed under the LLC laws of any state other than this state or an entity organized under the laws of any foreign country, as defined.

THIS BILL

This bill would expand the definition of a foreign LLC to include an LLC formed under the laws of a federally recognized Indian tribe. This would allow an LLC organized under tribal law to be able to qualify to do intrastate business within the state. It would also require an LLC formed under the laws of a federal recognized Indian tribe to pay the annual tax and fee imposed on foreign LLCs not classified as a corporation if it was doing business in this state or qualified to do business in this state.

IMPLEMENTATION CONSIDERATIONS

Implementing this bill would not significantly impact the department's programs and operations.

LEGISLATIVE HISTORY

SB 392 (Correa, 2009/2010) would allow a contractor to form an LLC and authorize the issuance of a contractor's license to an LLC under the Business and Professions Code. SB 392 is currently in the Senate Appropriations Committee. SB 1337 (Correa, 2007/2008) was identical to SB 392 and it failed passage out of the Senate Judiciary Committee.

AB 2235 (Parra, 2005/2006) would have expanded the definition of "person" under the Real Estate Law to include an LLC. This bill failed passage in the Senate Judiciary Committee without being heard.

SB 1022 (Campbell, 2005/2006) sought to authorize the formation of professional LLCs to provide professional services, as defined. This bill failed passage in the Senate Judiciary Committee.

AB 2724 (Runner, 2001/2002) would have authorized a contractor's license to be issued an LLC that met certain requirements. That bill failed passage out of the Assembly Business and Professions Committee.

OTHER STATES' INFORMATION

The states surveyed include *Florida, Illinois, Massachusetts, Michigan, Minnesota, and New York*. These states were selected due to their similarities to California's economy, business entity types, and tax laws.

Florida, Illinois, Massachusetts, Michigan, Minnesota, and New York laws allow LLCs formed under the laws of a federally recognized Indian tribe to form foreign LLCs.

FISCAL IMPACT

This bill would not significantly impact the department's costs.

ECONOMIC IMPACT

Revenue Estimate

This bill would result in the following revenue gains.

Estimated Revenue Impact of SB 653 As Amended May 6, 2009 Foreign Limited Liability Companies – Indian Tribes Enactment Assumed After June 30, 2009		
2009-10	2010-11	2011-12
+\$145,000	+\$145,000	+\$145,000

This analysis does not consider the possible changes in employment, personal income, or gross state product that could result from this bill.

Revenue Discussion

The revenue impact for this bill would be determined by the number of LLCs recognized under tribal law and request a file number from the SOS to form a foreign LLC in California.

According to the Bureau of Indian Affairs, there are 562 federally recognized American Indian tribes and Alaska Natives in the United States. Approximately 100 federally recognized Indian tribal governments currently exist in California.

According to the Legislative Analyst Office, there are approximately 60 Indian tribal casino operations in California. It is assumed that 50 percent of these casinos have ancillary businesses such as gas stations, hotels, and restaurants and that each of these casinos has an average of five ancillary business operations. This would result in approximately 150 ancillary businesses formed under tribal law [(60 Indian tribal casinos x 5 ancillary business operations) x 50% casinos with ancillary businesses]. It is estimated that there would be approximately 210 gaming and ancillary business operations formed under tribal law (150 ancillary businesses + 60 Indian tribal casinos). Assuming that 50 percent of these tribal business entities form LLCs under tribal law, there would be approximately 100 LLCs formed under tribal law (210 total gaming operations x 50%).

It is assumed that there are approximately 100 LLCs formed under tribal law in California, and that approximately one foreign LLC for every tribal LLC would apply for a file number with the SOS for a total of 100 foreign tribal LLCs (100 tribal LLCs x 1 foreign tribal LLC). The projected revenue generated from foreign tribal LLCs that pay the LLC annual tax would be \$80,000 (\$800 annual tax x 100 foreign tribal LLCs) in tax year 2010. It is assumed that this bill would be enacted late in 2009. Therefore, tax year 2010 would be assumed the initial year that tribal LLCs would form a foreign LLC and request a file number from the SOS. This would also be the first year that there the \$800 annual tax payment and the LLC fee would be due.

The LLC fee is determined based on the total gross income from California sources. Department data indicates approximately 70 percent of the California LLCs have less than \$249,999 of gross receipts. Because most of these LLCs recognized under tribal have a majority of their income derived from tribal land, it is assumed that 85 percent of foreign tribal LLCs have less than \$249,999 of California sourced gross receipts. As a result, it is estimated that 85 (100 tribal LLCs x 85%) foreign tribal LLCs would not be subject to the LLC fee. The remaining 15 percent or 15 of these foreign tribal LLCs (100 tribal LLCs x 15%) would have California source income of \$250,000 or more. It is assumed that the fee paid by these foreign tribal LLCs would be equal to the average fee paid by LLCs that paid a fee in 2007, approximately \$4,407. This would result in a revenue gain of \$65,000 (15 foreign tribal LLCs x \$4,407 average fee) from LLC fees in tax year 2010.

Total revenue gain from the \$800 annual tax and LLC fee would be approximately \$145,000 (\$80,000 + \$65,000) in 2010. The revenue gain is assumed the same for future years.

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