



STATE OF CALIFORNIA
Franchise Tax Board

Commercial Cannabis Activity: Personal Income Tax Law – Business Expenses Report

Economic and Statistical Research Bureau

Purpose

This report is intended to fulfill the Franchise Tax Board's obligation under Assembly Bill 37 (Chapter 792, Statutes of 2019) which added Revenue and Taxation Code Section 17209 and included a requirement that the Franchise Tax Board annually report to the Legislature by July 31, the number and total dollar amount of deductions and credits claimed under this section for the most recent calendar year in which either the deductions or credits are allowed.

Prepared by the Staff of the
Franchise Tax Board
STATE OF CALIFORNIA

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Background

In 2016, Proposition 64 was approved by California voters. Proposition 64 legalized commercial adult-use of cannabis and imposed two specific taxes on cannabis, an excise tax to be paid by consumers and a stepped cultivation tax to be paid by growers/cultivators.

In 2019, Assembly Bill 37 (Chapter 792, Statutes of 2019) was enacted to provide tax equity to the cannabis industry and allow commercial cannabis licensees, reporting under the Personal Income Tax law, to claim deductions and credits available to other legal businesses in the state. SB 167 (statutes of 2024) amended this section to extend the repeal date to January 1, 2030.

Under federal law (Internal Revenue Code (IRC) section 280E), taxpayers in the cannabis industry may not deduct business expenses or claim credits for activities related to a controlled substance. With the adoption of Proposition 64 and the subsequent passage of Assembly Bill 37 (Chapter 792, Statutes of 2019), California Personal Income Tax Law (PITL) allowed sole proprietorships and partnerships to claim credits and deductions for business expenses paid or incurred during the taxable year in carrying on commercial cannabis activity.

Franchise Tax Board Statutory Reporting Requirements

Under Chapter 792 of the Statutes of 2019 (AB 37), the FTB is required to provide an annual report to the Legislature, on or before July 31, in which either the deductions or credits are allowed. The report is required to include:

- The number of deductions and credits claimed pursuant to Section 17209 of the Revenue and Taxation Code (RTC).
- The total dollar amount of deductions and credits claimed pursuant to Section 17209 of the RTC.

Data

Beginning on or after January 1, 2020, California allows taxpayers operating under the PITL to claim credits and deductions of business expenses paid or incurred during the taxable year in conducting commercial cannabis activity (under RTC section 17209).

Because there is no reliable method of identifying qualified taxpayers, such as a cannabis Principal Business Activity code, the FTB created the information reporting form FTB 4197, to capture the performance metrics identified by the Legislature as required for this report. When taxpayers file form FTB 4197, they voluntarily self-report the business information needed, however the form is not required to be filed to claim deductions or credits nor is there a penalty for failing to file form FTB 4197. Additionally, because many cannabis businesses are formed as partnerships, the business income and expenses flow-through to partners, and

the business activities are reported by taxpayers on their personal income tax returns. These personal income taxpayers may not have the information necessary to file and report deductions and credits allowed under RTC Section 17209.

Table 1 below contains data that has been processed as of April of 2025 for credits and deductions allowed for business expenses paid or incurred for taxable years 2022 through 2024. The data is based on taxpayers' self-reported tax return information. Table 1 shows that the number of taxpayers reporting credits and deductions falls below the amount required for disclosure.

Table 1: Total Credits and Deductions Allowed by Tax Year**

Tax Year	Number of Returns	Total Credits Allowed	Total Deductions Allowed
2022*	N/A	N/A	N/A
2023*	N/A	N/A	N/A
2024*	N/A	N/A	N/A

*The number of 2022, 2023, and 2024 tax year returns reporting data on cannabis activities is too small to be reported under state taxpayer privacy rules. Additionally, not all timely 2024 tax year returns have been processed as of this writing.

** Form FTB 4197 data processed through April of 2025.

Although we believe more taxpayers are claiming the credits and deductions allowed under Chapter 792, Statutes of 2019 (AB 37), the information processed to date continues to show that very few of these forms have been filed. The FTB will continue to undertake efforts to improve taxpayer awareness of the existence, purpose, and correct usage of form FTB 4197.