Franchise Tax Board's Guide to:

Common Forms of Ownership

As a new business owner, one of your most important decisions is determining what form of ownership will best meet your business needs. Selecting the best structure for your business should be a carefully planned process that is discussed with a qualified professional such as an enrolled agent, certified public accountant, or attorney who specializes in this area. In addition, as your business grows over time, you may want to evaluate if a new form of ownership should be used to achieve better results. Although there are many forms of ownership to choose from, this guide highlights the most common.

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Common Forms of Ownership

Sole Proprietorship

This is the simplest and most common form used when starting a new business. Sole proprietorships are set up to allow individuals to own and operate a business by themselves. A sole proprietor has total control, receives all profits from, and is responsible for taxes and liabilities of the business.

Key Features of a Sole Proprietorship:

- It is inexpensive to start a sole proprietorship.
- A sole proprietorship consists of an individual or a married couple. (Ownership by more than one individual or registered domestic partner (RDP) creates a partnership.)
- The business and the owner are one. There is no separate legal entity.
- The owner of the sole proprietorship controls the entire business.
- The sole proprietor is personally liable for all debts and actions of the business. Personal assets may be used to pay the debts of the business.
- The life of the sole proprietorship continues to exist until it goes out of business, or as long as the business owner is alive. Once the owner dies, the sole proprietorship no longer exists.

How to Form a Sole Proprietorship:

- A separate bank account should be established for your business.
- Depending on your business type and business needs, an evaluation of risk may need to be done. Consult an insurance professional and your attorney to determine if liability insurance is recommended or needed.
- Most cities and counties require a business license, various permits, and/or registration to do business within their city or county limits. If you are doing business in multiple cities or counties, you may be required to have multiple licenses. Contact the business licensing department of the city and/or county directly where your business will primarily be located for specific rules and regulations. The Governor's CalGold online database at **calgold.ca.gov**, the Governor's Office of Business and Economic Development (GO-Biz) at **business.ca.gov**, and the California Business Portal at **businessportal.ca.gov** all provide links and contact information to agencies that administer and

issue business licenses, permits, and registration requirements from all levels of government.

- Contact your local Chamber of Commerce or call the statewide Chamber of Commerce at 800.331.8877 for information for your area and referrals to other agencies.
- Small Business Development Centers (SBDCs) provide assistance to small businesses throughout the United States and its territories. SBDCs help entrepreneurs realize the dream of business ownership and help existing businesses remain competitive in a complex, ever-changing global marketplace. SBDCs are hosted by leading universities and state economic development agencies and are funded in part through a partnership with SBA. For more information on SBDCs go to **sbagov/tools/local-assistance/sbdc**.
- If required, register a fictitious name, also referred to as "Doing Business As" or DBA. Refer to Appendix 1 in this booklet for more information.
- No formation documents are required to be filed with the Secretary of State.

Tax Return Filing Guidelines for a Sole Proprietorship:

- Use a federal Schedule C, *Profit or Loss from Business* to report business income and expenses.
- If you operated more than one business as a sole proprietorship, use a separate Schedule C for each business.
- Report the net income or loss from the Schedule C on your California individual income tax return, Form 540, *California Resident Income Tax Return* or Form 540NR, *Nonresident or Part-Year Resident Income Tax Return*.
- Include a complete copy of your federal return, including Schedule C, with your California individual income tax return.
- There is no requirement to file a separate tax return for the business. The due date of the federal return (including Schedule C) is the same as your California individual income tax return (with a copy of your federal return and Schedule C), which is normally April 15.
- The tax rate of the return depends on your individual income tax rate.

Estimated Tax:

- California taxes are pay-as-you go.
- Estimated tax installment payments for individuals are due and payable on April 15, June 15, September 15 of the taxable year, and January 15 of the following taxable year.
- Individuals complete California Form 540-ES, *Estimated Tax for Individuals*, to report their estimated taxes.
- A sole proprietorship will include all sources of business and personal income, such as wage and investment income, when determining estimated tax payments.
- Generally, you must make estimated tax payments if you expect to owe at least $500 ($250 if married/RDP filing separately) in tax for the current year (after subtracting withholding and credits) and you expect your withholding and credits to be less than the smaller of:

1. 90 percent of the tax shown on your current tax return; or
2. 100 percent of the tax shown on your prior year tax return including Alternative Minimum Tax (AMT).

Withholding:

If you pay a California nonresident for services they performed for your business while they were in California, generally, you must withhold 7 percent on all payments that exceed $1,500 in a calendar year.

If you backup withhold for the Internal Revenue Service, you must also backup withhold for the Franchise Tax Board on California source income. Backup withholding applies to California residents and nonresidents who do not provide a taxpayer identification number or do not certify exemption from backup withholding when required.

For more information about withholding, refer to FTB PUB 1017, *Resident and Nonresident Withholding Guidelines*.

How to End a Sole Proprietorship:

- File a federal Schedule C with your federal return and file a California return, with copies of your federal return and Schedule C, for the year you go out of business, or the year of the sole proprietor's death.
- File tax returns for any delinquent tax years.
- Pay all outstanding tax liabilities and penalties.

- Notify all creditors, vendors, suppliers, clients, and employees of your intent to go out of business. If the sole proprietorship ends because of the death of the sole proprietor, creditors may be entitled to an additional notice in the event of a probate or trust administration. Consult with a probate attorney, if necessary.
- Close out business checking account and credit cards.
- Cancel any licenses, permits, and fictitious business names.
- Consider publishing a statement in a local newspaper of general circulation near your principal place of business that you are no longer in business.

General Partnership

A general partnership must have two or more persons engaged in a business for profit. The general partnership is not a separately taxed entity. It is considered a conduit where the profit or loss of the business flows through to the partners. Partnership income is taxed as income to the partners. Losses may be subject to limitations. The partners report their share of the partnership profit or loss on their individual income tax returns even if their share of those profits is not actually distributed to them.

The partners decide the entity's structure, allocation of profits and losses, and the timing and amount of distributions. A formal written partnership agreement is advisable. Partnerships are very flexible and offer a variety of possible ownership and management structures.

General partners are jointly and severally liable for all legal and financial obligations of the partnership and for all wrongful acts of any partner acting in the ordinary course of the partnership's business.

Key Features of a General Partnership:

- A general partnership is a flexible form of business and relatively easy to set up.
- A general partnership must have more than one owner, unlike a sole proprietorship.
- The cost to form a general partnership is normally less expensive than forming a corporation.
- The general partnership does not pay income tax. A partnership is considered a pass-through entity, meaning that each partner's share of the partnership's profits, losses, deductions, credits, etc., will pass-through to each individual partner and those items will be reported on each partner's tax return in accordance with their written agreement. Losses may offset income, but may be subject to limitations.
- A general partnership exists as long as the partners agree it will and as long as there are at least two partners. This is subject to limitations imposed by California law.

How to Form a General Partnership:

- A partnership is formed when two or more persons agree to carry on a business and/or other endeavor for profit.
- A formal written partnership agreement is advisable.
- *A Statement of Partnership Authority* (Form GP-1) may be filed with the Secretary of State at the option of the partners. This document specifies the authority, or limitations on the authority, of some or all of the partners to enter into transactions on behalf of the partnership and any other matter. The Secretary of State will assign a 12-digit filing number. Keep this filing number for your tax records. Contact the California Secretary of State at 916.657.5448 or go to **sos.ca.gov** for more information.
- The partners should establish a separate bank account in the name of the partnership for its financial operations.
- Partners should consider an evaluation of the types of risks the partnership might encounter in connection with its operations. Consultation with attorneys and insurance brokers in this area is advisable.
- Most cities and counties require a business license, various permits, and/or registration to do business within their city or county limits. If you are doing business in multiple cities or counties, you may be required to have multiple licenses. Contact the business licensing department of the city and/or county directly where your business will primarily be located for specific rules and regulations. The Governor's CalGold online database at **calgold.ca.gov**, the Governor's Office of Business and Economic Development (GO-Biz) at **business.ca.gov**, and the California Business Portal at **businessportal.ca.gov** all provide links and contact information to agencies that administer and issue business licenses, permits, and registration requirements from all levels of government.
- Contact your local Chamber of Commerce or call the statewide Chamber of Commerce at 800.331.8877 for information for your area and referrals to other agencies.
- If required, register a fictitious name, also referred to as "Doing Business As" or DBA, refer to Appendix 1 in this booklet for more information.

Tax Return Filing Guidelines for a General Partnership:

- Every general partnership that engages in a trade or business in California or earns income from California sources must file an informational return, California Form 565, *Partnership Return of Income*.
- Generally, the due date of the Form 565 is the 15th day of the 3rd month after the close of the general partnership's taxable year.
- The general partnership's items of income, deductions, and credits flow through the partnership to its partners and are reported on the California Schedule K-1 (565), *Partner's Share of Income, Deductions, Credits, etc*.
- The general partnership provides each partner with a Schedule K-1 (565) that states the partner's distributive share of the general partnership's items of income, deductions, and credits even if they are not actually distributed.

Estimated Tax:

The general partnership has no estimated tax requirements. However, California taxes are pay-as-you-go, so partners may have to make estimated tax payments for their own reporting purposes.

- An individual partner's estimated tax installment payments are due and payable on April 15, June 15, September 15 of the taxable year, and January 15 of the following taxable year.
- Individual partners complete California Form 540-ES, *Estimated Tax for Individuals* to report their estimated taxes.
- Generally, you must make estimated tax payments if you expect to owe at least $500 ($250 if married/RDP filing separately) in tax for the current year (after subtracting withholding and credits) and you expect your withholding and credits to be less than the smaller of:
  1. 90 percent of the tax shown on your current tax return; or
  2. 100 percent of the tax shown on your prior year tax return including Alternative Minimum Tax (AMT).
- Each partner is responsible for paying taxes on his/her distributive share even if it is not actually distributed.

Withholding:

General partnerships must withhold 7 percent on distributions of California source income made to domestic nonresident partners when distributions to a particular partner exceed $1,500 for the calendar year.

If the general partnership pays a nonresident independent contractor for services performed in California, normally, the general partnership must withhold 7 percent on all payments that exceed $1,500 in a calendar year.

If the general partnership is required to backup withhold for the Internal Revenue Service, it must also backup withhold for the Franchise Tax Board on California source income. Backup withholding applies to California residents and nonresidents who do not provide a taxpayer identification number or do not certify exemption from backup withholding when required.

For more information about partnership withholding, refer to FTB PUB 1017, *Resident and Nonresident Withholding Guidelines*.

How to End a General Partnership:

- File California Form 565 for all required tax years (including any delinquent returns) and pay all outstanding tax liabilities, penalties, and interest.
- If the general partnership filed a *Statement of Partnership Authority* (Form GP-1) with the Secretary of State, it should complete a *Statement of Dissolution* (Form GP-4) and file it with the Secretary of State. This will put the public on notice that the partnership has been dissolved.
- Notify all creditors, vendors, suppliers, clients, and employees of the general partnership's intent to go out of business.
- Close out business checking account and credit cards.
- Cancel any licenses, permits, and fictitious business names.
- Consider publishing a statement in a local newspaper of general circulation near the general partnership's principal place of business that it is no longer in business.

Limited Partnership

Limited partnerships are formed by two or more people, with at least one person acting as the general partner who has management authority and personal liability, and at least one person in the role of limited partner. All partners – both general and limited – must enter into limited partnership by either oral or written agreement. A formal written partnership agreement is advisable.

Limited partnerships are managed and controlled by one or more general partners; general partners have authority to bind the partnership. Limited partners normally do not participate in managing the business.

The general partners are liable for partnership obligations to the same extent as partners of general partnerships. Limited partners, however, are generally not liable for the partnership's obligations; their only risk is their agreed capital contribution, or as otherwise provided in the partnership agreement. However, if limited partners participate in the management of the partnership business, they may lose their protected limited partner status and become liable to the same extent a general partner is.

Key Features of a Limited Partnership:

- A limited partnership is a flexible form of business and relatively easy to set up.
- A limited partnership allows for more than one owner, unlike a sole proprietorship.
- A limited partnership involves two or more people who agree to create a business and share in its profits and losses.
- The partners decide the structure of the entity, the allocation of profits and losses, and the timing and amount of distributions.
- The general partner is responsible for managing the business affairs.
- The limited partner typically provides only capital, such as cash, to the partnership.
- Each general partner assumes full personal liability for the debts and obligations of the partnership.
- The limited partner's liability is normally limited to their investment in the partnership.

- A limited partnership exists, subject to limitations imposed by California law, as long as the partners agree it will and as long as there are at least two partners, one of which is a general partner and one of which is a limited partner.
- The limited partnership does not pay income tax.
- A limited partnership pays an annual tax of $800 to California.

How to Form a Limited Partnership:

To form a limited partnership, a *Certificate of Limited Partnership* (Form LP-1) must be filed with the California Secretary of State. A limited partnership formed in another state must register with the California Secretary of State by filing an *Application to Register* (Form LP-5) and attaching a completed form of valid certificate of good standing prior to conducting business in the state. The Secretary of State will assign a 12-digit filing number. Keep this filing number for your tax records. Contact the California Secretary of State at 916.657.5448 or go to **sos.ca.gov** for more information.

- A separate bank account should be established for the limited partnership.
- A formal written limited partnership agreement is advisable.
- The limited partnership should consider purchasing insurance to cover the risks of running the business. Consultation with a business attorney and an insurance specialist on the matter is advisable.
- Most cities and counties require a business license, various permits, and/or registration to do business within their city or county limits. If you are doing business in multiple cities or counties, you may be required to have multiple licenses. Contact the business licensing department of the city and/or county directly where your business will primarily be located for specific rules and regulations. The Governor's CalGold online database at **calgoldca.gov**, the Governor's Office of Business and Economic Development (GO-Biz) at **business.ca.gov**, and the California Business Portal at **businessportal.ca.gov** all provide links and contact information to agencies that administer and issue business licenses, permits, and registration requirements from all levels of government.
- Contact your local Chamber of Commerce or call the statewide Chamber of Commerce at 800.331.8877 for information for your area and referrals to other agencies.

- If required, register a fictitious name, also referred to as "Doing Business As" or DBA. Refer to Appendix 1 in this booklet for more information.

Tax Return Filing Guidelines for a Limited Partnership:

- Every limited partnership that is formed in California or registered with the California Secretary of State must file California Form 565, *Partnership Return of Income* even if it has no income from California sources.
- Every limited partnership that engages in a trade or business in California or earns income from California sources must file an informational return, Form 565.
- Generally, the due date of the Form 565 is the 15th day of the 3rd month after the close of the partnership's taxable year.
- A limited partnership must pay an annual tax of $800 to California.
- The limited partnership's items of income, deductions, and credits flow through each partner's limited partnership to its partners and are reported on each partner's California Schedule K-1 (565), *Partner's Share of Income, Deductions, Credits, etc*. even if they are not actually distributed.
- The limited partnership provides each partner with a Schedule K-1 (565) that states the partner's distributive share of the partnership's items of income, deductions, and credits.

Estimated Tax:

The limited partnership has no estimated tax requirements. However, California taxes are pay-as-you-go, so partners may have to make estimated tax payments for their own reporting purposes.

- Generally, both the limited and general partners' estimated tax installment payments are due and payable on April 15, June 15, September 15 of the taxable year, and January 15 of the following taxable year.
- Individuals complete California Form 540-ES, *Estimated Tax for Individuals* to report their estimated taxes.

- Generally, you must make estimated tax payments if you expect to owe at least $500 ($250 if married/RDP filing separately) in tax for the current year (after subtracting withholding and credits) and you expect your withholding and credits to be less than the smaller of:
  1. 90 percent of the tax shown on your current tax return; or
  2. 100 percent of the tax shown on your prior year tax return including Alternative Minimum Tax (AMT).
- Each limited and general partner is responsible for paying taxes on their distributive share even if they are not actually distributed.

Withholding:

Limited partnerships must withhold 7 percent on distributions of California source income made to domestic nonresident partners when distributions to a particular partner exceed $1,500 for the calendar year.

If the limited partnership pays a nonresident independent contractor for services performed in California, generally, the limited partnership must withhold 7 percent on all payments that exceed $1,500 in a calendar year.

If the limited partnership is required to backup withhold for the Internal Revenue Service, it must also backup withhold for the Franchise Tax Board on California source income. Backup withholding applies to California residents and nonresidents who do not provide a taxpayer identification number or do not certify exemption from backup withholding when required.

For more information about limited partnership withholding, see FTB PUB 1017, *Resident and Nonresident Withholding Guidelines*.

How to End a Limited Partnership:

- File California Form 565 for the last taxable year, check the box that indicates that it is a final return, and write "Final" on top of the return.
- File California Form 565 for all delinquent tax years.
- Pay all outstanding tax liabilities, penalties, and interest.
- Publish notice of its dissolution requesting persons with claims against it to present them (see California Corporations Code Section 15908.07).

- Dispose of known claims by following the procedures specified in California Corporations Code Section 15908.06.
- File a *Certificate of Cancellation* (Form LP-4/7) with the California Secretary of State.
- Notify all creditors, vendors, suppliers, clients, and employees of its intent to go out of business.
- Close out business checking accounts and credit cards.
- Cancel any licenses, permits, and fictitious business names.
- Consider publishing a statement in a local newspaper of general circulation near the principal place of business that the limited partnership is no longer in business.
- Refer to FTB PUB 1038, *Guide to Dissolve, Surrender, or Cancel a California Business Entity* for more information on how to cancel a limited partnership.

Corporation

A corporation is a business entity formed under state civil law that is a separate legal entity owned by shareholders.

The California Corporations Code contains general provisions for the formation of many different types of corporations such as personal service corporations, benefit corporations, social purpose corporations, nonprofit corporations, and corporations for various special purposes (such as cooperative corporations). Consult an attorney, specializing in business entity matters, for advice about which type of corporation should be used for your specific business needs.

A corporation is managed by or under the direction of a board of directors, which generally determines corporate policy. Officers manage the day-to-day affairs of the corporation. Corporations issue stock to their owners (the shareholders). Shareholders, unless they are officers, do not participate in day-to-day management activities. Management structure can be altered by committees of board members and shareholder agreements. Shareholders generally are not personally liable for obligations of the corporation.

Key Features of a Corporation:

- Generally, the life of the corporation is perpetual in nature.
- Generally, ownership is easily transferred through the sale of stock, and new owners can be easily added by issuing additional stock.
- It is more costly to set up and maintain than a sole proprietorship or partnership.
- The corporation must create bylaws (i.e., how the corporation will operate) that cover items such as stockholder and director meetings, the number of officers, and their responsibilities.
- To preserve the liability protection for its owners, a corporation is required to abide by numerous corporate formalities, including but not limited to the holding of annual meetings and the keeping of written minutes.
- Each year, the corporation must file a *Statement of Information* with the Secretary of State.

- Generally, owners (shareholders) are not liable for the corporation's contractual debts and other obligations and creditors may only look to the corporation and the business assets for payment. However, there are some exceptions. For example, if an owner/shareholder becomes a guarantor or cosigner of a debt, they may be liable.
- A separate bank account and separate records are required.
- The corporation pays a minimum tax of $800 each taxable year.
- The California $800 minimum tax is waived on newly formed or qualified corporations filing an initial return for their first taxable year.
- The California $800 minimum tax is also waived if the corporation (1) did not do business in California during the taxable year, and (2) the taxable year was 15 days or fewer.

How to Form a Corporation:

The type of corporation you form will affect the administration and operation of the corporation and the type of documents that must be filed with the Secretary of State. The Secretary of State will assign a 7-digit filing number and the date of incorporation. Keep this filing number and date for your tax records. Contact the California Secretary of State at 916.657.5448 or go to **sos.ca.gov** for more information.

- A separate bank account should be established for the corporation.
- A corporation formed in California, referred to as a domestic corporation, will file the appropriate *Articles of Incorporation* and pay a fee to the Secretary of State. When a corporation is formed somewhere other than California, referred to as a foreign corporation, it can qualify/register to transact business in California by filing the appropriate *Statement and Designation by Foreign Corporation* along with an official certificate that verifies the corporation exists in good standing with the country or state of its incorporation, and pay a fee to the California Secretary of State.
- A corporation must create bylaws (i.e., how the corporation will operate) that cover items such as stockholder and director meetings, the number of officers, and their responsibilities.

- The California Corporation Code requires a corporation to hold annual meetings and keep written minutes to preserve the liability shield for its owners. Note: additional corporate formalities may also be necessary to preserve liability protections. The performance or omission of certain acts may eliminate the liability shield for the shareholders. Consult with a business attorney, if necessary.
- Corporations are also required to file a *Statement of Information* with the California Secretary of State every year. If the *Statement of Information* is not timely filed, the corporation may be subject to penalties and/or may be suspended. Contact the California Secretary of State at 916.657.5448 or go to **sos.ca.gov** for more information.
- Most cities and counties require a business license, various permits, and/or registration to do business within their city or county limits. If you are doing business in multiple cities or counties, you may be required to have multiple licenses. Contact the business licensing department of the city and/or county directly where your business will primarily be located for specific rules and regulations. The Governor's CalGold online database at **calgold.ca.gov**, the Governor's Office of Business and Economic Development (GO-Biz) at **business.ca.gov**, and the California Business Portal at **businessportal.ca.gov** all provide links and contact information to agencies that administer and issue business licenses, permits, and registration requirements from all levels of government.
- Contact your local Chamber of Commerce or call the statewide Chamber of Commerce at 800.331.8877 for information for your area and referrals to other agencies.
- If required, register a fictitious name, also referred to as "Doing Business As" or DBA. Refer to Appendix 1 in this booklet for more information.

Personal Service Corporation

A personal service corporation is a type of corporation whose principal business activity is the performance of personal services and such services are performed by employee-owners. Individuals who perform services in fields such as health, law, engineering, architecture, performing arts, and accounting typically use this classification.

A corporation is a personal service corporation if it meets all of the following requirements:

1. Its principal activity during the testing period is performing personal services. Personal services include any activity performed in the fields of accounting, actuarial science, architecture, consulting, engineering, health (including veterinary services), law, and the performing arts. Generally, the testing period for any tax year is the prior tax year. If the corporation has just been formed, the testing period begins on the first day of its tax year and ends on the earlier of:
   - The last day of its tax year, or
   - The last day of the calendar year in which its tax year begins.
2. Its employee-owners substantially perform the personal services. This requirement is met if more than 20 percent of the corporation's compensation cost for its activities of performing personal services during the testing period is for personal services performed by employee-owners.
3. Its employee-owners own more than 10 percent of the fair market value of its outstanding stock on the last day of the testing period.

A person is an employee-owner of a personal service corporation if both of the following apply:

- The individual is an employee of the corporation or performs personal services for, or on behalf of, the corporation (even if the individual is an independent contractor for other purposes) on any day of the testing period.
- The individual owns any stock in the corporation at any time during the testing period.

Benefit Corporation

A benefit corporation is a new type of corporation that voluntarily meets higher standards of corporate purpose, accountability, and transparency. A corporation is a benefit corporation if it meets all of the following requirements:

1. It has a corporate purpose to create a general public benefit or a material positive impact on society and the environment.
2. It is required to provide greater protection to its officers and directors to pursue objectives that benefit society, the environment, and the corporation's employees.
3. It is required to make available to the public an annual benefit report that assesses their overall social and environmental performance against a third party standard.

Social Purpose Corporation

A social purpose corporation (SPC) is very similar to a benefit corporation in its standards and requirements. There is a slight difference in its accountability and reporting requirements as an SPC does not have an independent third party standard to assess the company's social and environmental performance.

More information on both benefit corporations and SPCs is available at **sos.ca.gov** and **ftb.ca.gov.**

Nonprofit Corporation

A nonprofit corporation is a corporation that is formed to carry out charitable, educational, religious, literary, scientific, social, or other similar purposes. They are formed pursuant to the Nonprofit Corporation Law in the California Corporations Code. A nonprofit corporation does not pay federal or state income taxes on profits from activities it engages in to carry out its objectives if it is tax-exempt. In order to qualify for this special tax-exempt status, it must apply for it with the Internal Revenue Service and the Franchise Tax Board. More information on nonprofit corporations is available at **sos.ca.gov**, **ftb.ca.gov**, and FTB PUB 927, *Introduction to Tax-Exempt Status*.

Tax Return Filing Guidelines for a Corporation:

Corporations are normally taxed under Internal Revenue Code, Subtitle A, Chapter 1, Subchapter C. Corporations taxed following the Subchapter C rules are more commonly known as "C corporations." They are taxed annually on their earnings and the shareholders pay tax on these earnings when distributed as dividends.

The California Revenue and Taxation code requires a C corporation to be subject to the $800 minimum franchise tax if it is incorporated or organized in the state (domestic corporations); qualified or registered to do business in the state (foreign corporations); or doing business in the state without having incorporated, organized, or registered/qualified.

Tax Return Filing Guidelines for a C Corporation:

- C corporations that organize in California, register in California, conduct business in California, or receive California source income must file California Form 100, *California Corporation Franchise or Income Tax Return*.

- The C corporation's return due date is the 15th day of the 4th month after the close of the taxable year.
- C corporations are taxed on their net income at a rate of 8.84 percent by California.
- C corporations are subject to a California minimum tax of $800.
- The California $800 minimum franchise tax is due the first quarter of each accounting period and must be paid whether the corporation is active, inactive, operates at a loss, or files a return for a short period of less than 12 months.
- The California $800 minimum tax is waived on newly formed or qualified corporations filing an initial return for their first taxable year. The California $800 minimum tax is also waived if the corporation (1) did not do business in California during the taxable year, and (2) the taxable year was 15 days or fewer.

Estimated Tax for a C Corporation:

California taxes are pay-as-you-go, so C corporations may have to make estimated tax payments for their own reporting purposes.

- The C corporations estimated tax is due and payable in four installments on April 15, June 15, September 15, and December 15.
- C corporations complete and file California Form 100-ES, *Corporation Estimated Tax* to report their estimated taxes. (For more information and applicable rates, go to **ftb.ca.gov/forms**, and search for **100-ES**.)
- The California $800 minimum franchise tax is due the first quarter of the C corporation's accounting period and must be paid whether the corporation is active, inactive, operates at a loss, or files a return for a short period of less than 12 months.

Tax Return Filing Guidelines for an S Corporation:

Corporations formed under state civil law (and other civil law business entities classified as a corporation for franchise/income tax purposes) may elect to be taxable as an "S corporation" for franchise and income tax purposes pursuant to the provisions of Internal Revenue Code, Subtitle A, Chapter 1, Subchapter S. A corporation makes the election to be taxable as an S corporation by filing IRS Form 2553, *Election by a Small Business Corporation* with the IRS. An entity that has a valid S corporation election in effect for federal income tax purposes is treated as an S corporation for California income/franchise tax purposes.

An S corporation is not subject to federal corporate income tax, with several exceptions. An S corporation is subject to federal income tax on excess net passive investment income. Also, an S corporation that was previously a C corporation is also subject to federal income tax on built-in gains recognized during the "recognition period" following the S election. Except for these limited cases where the S corporation is subject to federal income tax, the S corporation is a "pass-through entity" similar to an entity taxable as a partnership. Items of income, gain, deduction, and credit pass through to the S corporation's shareholder(s) on a pro rata ownership basis. These S corporation items are included in the federal income of the shareholder(s), subject to provisions that limit the pass-through of losses and deductions, for purposes of determining a shareholder's federal income tax.

California generally applies the federal income tax rules to S corporations. However, California differs from federal tax law by also imposing a general corporate franchise or income tax on S corporations, but at a tax rate of only 1.5 percent (3.5 percent for financial S corporations).

Key tax features of an S corporation include:

- The number of shareholders may not exceed 100.
- The corporation can have only one class of stock.
- Ownership is generally limited to individuals who are U.S. citizens or residents, certain tax-exempt entities, and certain types of trusts. Partnerships, corporations (other than certain tax-exempt corporations), and nonresident alien individuals are not allowed as shareholders.
- An entity elects to be an S corporation by filing Form 2553 with the IRS. An entity that is an S corporation for federal purposes is an S corporation for California purposes.
- Detailed rules apply to the timing and other requirements for making and revoking a valid election to be taxable as an S corporation, and for what causes a termination of an election.
- An S corporation generally does not pay federal income tax, with exceptions for tax on excess net passive investment income and on certain built-in gains.

- Under California law, the S corporation is subject to a 1.5 percent tax on its net income (3.5 percent for financial corporations).
- The items of income, deductions, and credits flow through from the S corporation to each shareholder through the Schedule K-1 (IRS 1120S/FTB 100S), *Shareholder's Share of Income, Deductions, Credits, etc*. Each shareholder is responsible for paying taxes on their pro rata share of the S corporation's items of income, deductions, and credits even if they are not actually distributed.

An entity taxable as an S corporation that organizes in California, registers in California, does business in California, or receives California source income must file Form 100S, *California S Corporation Franchise or Income Tax Return*.

The return due date is the 15th day of the 3rd month after the close of the taxable year.

S corporations are subject to the $800 minimum California franchise tax. The California $800 minimum tax is waived on newly formed or qualified corporations filing an initial return for their first taxable year. The California $800 minimum tax is also waived if the corporation (1) did not do business in California during the taxable year, and (2) the taxable year was 15 days or less.

The S corporation must provide each shareholder with a Schedule K-1 (IRS 1120S/FTB 100S) that states the shareholder's pro rata share of the S corporation's items of income, deductions, and credits even if no income is actually distributed.

Taxpayers that desire to do business as an S corporation should seek professional tax advice.

Estimated Tax for an S Corporation:

California taxes are pay-as-you-go. Therefore, S corporations and their shareholders may have to make estimated tax payments for their own separate reporting purposes.

- The S corporation's estimated tax is due and payable in four installments on April 15, June 15, September 15, and December 15.
- S corporations complete and file California Form 100-ES, *Corporation Estimated Tax* to report their estimated taxes. (For more information and applicable rates, go to **ftb.ca.gov/forms**, and search for **100-ES**.)
- The California $800 minimum franchise tax is due the first quarter of the S corporation's accounting period and must be paid whether the corporation is active, inactive, operates at a loss, or files a return for a short period of less than 12 months.

- An individual shareholder's estimated tax installment payments are due and payable on April 15, June 15, September 15 of the taxable year, and January 15 of the following taxable year.
- Individual shareholders complete California Form 540-ES, *Estimated Tax for Individuals* to report their estimated taxes.
- Generally, you must make estimated tax payments if you expect to owe at least $500 ($250 if married/RDP filing separately) in tax for the current year (after subtracting withholding and credits) and you expect your withholding and credits to be less than the smaller of:
  1. 90 percent of the tax shown on your current tax return; or
  2. 100 percent of the tax shown on your prior year tax return including Alternative Minimum Tax (AMT).
- Each shareholder is responsible for paying taxes on his/her pro rata share of S corporation income even if no money or property is actually distributed to the shareholders.

How to End a Corporation:

- File California Form 100 or Form 100S for the last taxable year, check the box that indicates that it is a final return, and write "Final" on top of the return.
- File California Form 100 or Form 100S for all delinquent tax years.
- Pay all outstanding tax liabilities, interest, and penalties.
- Domestic corporations file the appropriate *Certificate of Election to Wind Up and Dissolve*, with the California Secretary of State.
- Foreign corporations file the appropriate *Certificate of Surrender of Right to Transact Intrastate Business* with the California Secretary of State.
- Notify all creditors, vendors, suppliers, clients, and employees of your intent to go out of business.
- Close out business checking account and credit cards.
- Cancel any licenses, permits, and fictitious business names.
- Consider publishing a statement in a local newspaper of general circulation near the principal place of business that the corporation is no longer in business.
- Refer to FTB PUB 1038, *Guide to Dissolve, Surrender, or Cancel a California Business Entity* for more information on how to dissolve a corporation.

Limited Liability Company

A Limited Liability Company (LLC) is a hybrid entity that may have some advantages over corporations and partnerships depending on your business needs. The LLC's main advantage over a partnership is that, like the owners (shareholders) of a civil law corporation, the liability of the owners (members) of an LLC is limited to their financial investment. However, like a general partnership, members of an LLC have the right to participate in management of the LLC, unless the LLC's articles of organization and operating agreement provide that managers will manage the LLC.

Key Features of an LLC:

- An LLC may have one or more owners, and may have different classes of owners.
- An LLC may be owned by any combination of individuals or business entities.
- An LLC may not be formed under state civil law to conduct a business that requires a professional license to operate, for example, a lawyer may not form an LLC. However, there may be certain exceptions to this rule.
- An LLC may be taxable as a sole proprietorship, partnership, C corporation, or S corporation.
- An LLC that is taxable as a partnership can achieve both conduit tax treatment and limited liability protection under civil law.
- An LLC taxable as a partnership does not have the ownership restrictions that apply to entities taxable as S corporations.
- If the LLC has a single member, it will be disregarded as separate from its owner, and will be treated as a sole proprietorship or a division of its owner, unless it elects to be taxable as a corporation.
- In general, all the owners (members) are shielded from individual liability for debts and obligations of the LLC.
- Forming and maintaining an LLC may be simpler and faster than forming and maintaining a civil law corporation.
- An LLC is typically managed by all its members, unless the members agree to have a manager handle the LLC's business affairs.
- An LLC's life is perpetual in nature. However, the members may agree to a date or event of termination.

How to Form an LLC:

A California LLC is formed by filing articles of organization with the California Secretary of State prior to conducting business. A foreign (out-of-state or out-of country) LLC that conducts business in California is subject to the California tax filing requirements. A foreign LLC should check with their state of origin for entity requirements.

The LLC members must enter into a verbal or written operating agreement. A formal, written agreement is advisable. The LLC does not file the operating agreement with the Secretary of State but maintains it at the office where the LLC's records are kept.

An LLC may be managed by managers who are not members, if provided for in the articles of the organization. However, if the LLC is managed by managers, they alone have authority to bind the LLC; members and directors have no authority in these matters. Otherwise, the LLC is managed by its members. In this case, every member is an agent of the LLC and has the power to bind the LLC and the right to vote on merger or dissolution. Members of the LLC have the same degree of limited liability as a shareholder of a corporation. The Secretary of State will assign a 12-digit filing number and the date of organization. Keep this filing number and date for your tax records. Contact the California Secretary of State at 916.657.5448 or go to **sos.ca.gov** for more information.

- A separate bank account should be established for the LLC.
- An LLC formed in California, referred to as a California LLC, will file the appropriate *Articles of Organization* and pay a fee to the Secretary of State prior to conducting business. When an LLC is formed somewhere other than California, referred to as a foreign LLC, it can register to transact business in California by filing the appropriate *Application to Register a Foreign Limited Liability Company* along with an official certificate that verifies the LLC exists in good standing with the agency where it was formed, and pay a fee to the California Secretary of State.
- LLCs are only required to file the *Statement of Information* biannually (every two years) with the Secretary of State. LLCs do not issue stock, or have to hold annual meetings and keep written minutes to preserve the liability shield for its owners. An election to be classified as a corporation for tax purposes will not change these requirements.

- Most cities and counties require a business license, various permits, and/or registration to do business within their city or county limits. If you are doing business in multiple cities or counties, you may be required to have multiple licenses. Contact the business licensing department of the city and/or county directly where your business will primarily be located for specific rules and regulations. The Governor's CalGold online database at **calgold.ca.gov**, the Governor's Office of Business and Economic Development (GO-Biz) at **business.ca.gov**, and the California Business Portal at **businessportal.ca.gov** all provide links and contact information to agencies that administer and issue business licenses, permits, and registration requirements from all levels of government.
- Contact your local Chamber of Commerce or call the statewide Chamber of Commerce at 800.331.8877 for information for your area and referrals to other agencies.
- If required, register a fictitious name, also referred to as "Doing Business As" or DBA. Refer to Appendix 1 in this booklet for more information.

Tax Return Filing Guidelines for an LLC:

For income tax purposes, California treats the LLC and its owners, in the same manner the LLC is treated for federal tax purposes. An LLC with a single member is classified as a sole proprietorship, while an LLC with more than one member is classified as a partnership, unless the LLC chooses to be classified as a corporation for income tax purposes. To be taxed as a corporation, the LLC files an election on a federal Form 8832, *Entity Classification Election* with the Internal Revenue Service.

A California LLC which has members who are not residents of California must file FTB 3832, *Limited Liability Company Nonresident Members' Consent* with California Form 568, *Limited Liability Return of Income*. FTB 3832 is signed by the nonresident individuals and foreign entity members to show their consent to California's jurisdiction to tax their distributive share of income attributable to California sources. The LLC must pay the tax for every nonresident member that did not sign FTB 3832.

Single Member LLC

Although California tax law requires an LLC to have the same tax classification for both state and federal tax purposes, filing requirements differ. For federal tax purposes, there is no separate reporting requirement for the disregarded single member LLC (SMLLC). Reporting the activities of the disregarded SMLLC on the single-member's federal income tax return is sufficient. However, for California tax purposes, disregarded SMLLCs that are organized or doing business in California, or are registered with the California Secretary of State are required to:

- File California Form 568 and also include:
  - *Single Member LLC Information and Consent* section on Side 3.
  - Schedule IW, *Limited Liability Company* (LLC) *Income Worksheet*.
  - Schedule B and Schedule K when any item of income, profit, gain, or distribution is $3 million or more.
  - $800 annual tax.
  - LLC fee, if applicable.

The disregarded SMLLC is not required to issue a Schedule K-1 to a single-member.

The disregarded SMLLC's tax return, Form 568, is due by the 15th day of the 4th month after the close of the tax year. If the disregarded SMLLC files its tax return under the automatic six-month extension, then the due date is the 15th day of the 10th month after the close of the tax year. The disregarded SMLLC will use the same tax year as its single-member. Generally, individuals adopt a calendar year as their tax year, so the due date for the disregarded SMLLC is often April 15 and the extended due date is October 15.

The due date for the $800 annual tax is the same as the original due date for the LLC tax return, not the extended due date. For many disregarded SMLLCs this means the $800 annual tax is due April 15.

FTB 3537, *Payment for Automatic Extension for LLCs* is used to pay the disregarded SMLLC's tax and fee by the original due date of the disregarded SMLLC's tax return.

If the disregarded SMLLC's only member is a nonresident who has not signed the *Single Member LLC Information and Consent* on Side 3 of the Form 568, then the disregarded SMLLC is required to complete Schedule T, located on Side 4 of the Form 568 and pay the tax on behalf of its single owner. Payment is due by the original due date of the disregarded SMLLC's tax return. Use FTB 3537 to make this payment.

The LLC fee is based on the LLC's total income from all sources derived from or attributable to California. It is determined as follows:

If Total Income is:	Fee:
$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

The LLC fee is generally considered an ordinary and necessary expense paid or incurred in carrying on the LLC's trade or business. The fee is deductible on the LLC's Form 568, *Schedule B*, on the Other Deductions line.

The estimated LLC fee is due by the 15th day of the 6th month of the taxable year. The due date for the estimated LLC fee is often June 15. Use FTB 3536, *Estimated Fee for LLCs*, to make the estimated LLC fee payment.

The person who owns a disregarded SMLLC that operates a trade or business may be subject to the tax on net earnings from self-employment in the same manner as a sole proprietorship and responsible to make quarterly estimated tax payments. For more information, refer to IRS Publication 3402, *Taxation of Limited Liability Companies*, and California Form 540-ES, *Instructions for Estimated Taxes for Individuals* for more information.

Estimated Tax for an SMLLC:

- California taxes are pay-as-you go.
- The due date for the $800 annual tax is the same as the original due date for the LLC tax return, not the extended due date. For many disregarded SMLLCs this means the $800 annual tax is due April 15.
- Estimated tax installment payments for the individual SMLLC are due and payable on April 15, June 15, September 15 of the taxable year, and January 15 of the following taxable year.
- Individuals complete California Form 540-ES, *Estimated Tax for Individuals* to report their estimated taxes.
- An individual who is the single member of the LLC will include all sources of business and personal income, such as wage and investment income, when determining estimated tax payments.

- Generally, you must make estimated tax payments if you expect to owe at least $500 ($250 if married/RDP filing separately) in tax for the current year (after subtracting withholding and credits) and you expect your withholding and credits to be less than the smaller of:
  1. 90 percent of the tax shown on your current tax return; or
  2. 100 percent of the tax shown on your prior year tax return including Alternative Minimum Tax (AMT).

Withholding for an SMLLC:

If the SMLLC pays a California nonresident for services they performed for the business while they were in California, generally, the SMLLC must withhold 7 percent on all payments that exceed $1,500 in a calendar year.

If you backup withhold for the Internal Revenue Service, you must also backup withhold for the Franchise Tax Board on California source income. Backup withholding applies to California residents and nonresidents who do not provide a taxpayer identification number or do not certify exemption from backup withholding when required.

For more information about withholding, refer to FTB PUB 1017, *Resident and Nonresident Withholding Guidelines*.

LLC Classified as Partnership

Known as the "default rule," Treasury Regulation Section 301.77013(f)(2), provides that an LLC with at least two members is classified as a partnership for federal tax purposes. If an LLC with two or more members chooses the default rule of partnership classification for federal purposes, it must follow the federal partners and partnerships rules found in Internal Revenue Code (IRC) Subchapter K (IRC Sections 701-777), to which California conforms through Revenue and Taxation Code Section 17851. The partnership rules give the multiple-member LLC a significant amount of flexibility to vary their respective shares of the members' income. The multiple-member LLC will also be in a position to make the tax elections at the entity level, rather than the member level. Such elections may include selecting a tax year, adopting accounting and depreciation methods, and to amortize organizational costs. For more information, refer to IRS Publication 541, *Partnerships*.

The multiple-member LLC will file as a partnership for federal tax purposes (unless it makes an affirmative election to be classified as a corporation for federal tax purposes) using IRS Form 1065, *U.S. Return of Partnership Income*.

However, for California tax purposes the Form 568, *Limited Liability Return of Income*, not the California Form 565, *Partnership Return of Income* is filed by a multiple-member LLC organized or doing business in California. The Form 568 is also filed by the LLC classified as a partnership when it has California source income or is registered with the California Secretary of State.

The $800 annual tax and LLC fee, as detailed in the SMLLC section above, are also imposed on the multiple-member LLC's total income from all sources derived from or attributable to California when the partnership federal tax classification is used by the LLC.

The LLC fee is based on the LLC's total income from all sources derived from or attributable to California. It is determined as follows:

If Total Income is:	Fee:
$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

The LLC fee is generally considered an ordinary and necessary expense paid or incurred in carrying on the LLC's trade or business. The fee is deductible on the LLC's Form 568, *Schedule B*, on the Other Deductions line.

The estimated LLC fee is due by the 15th day of the 6th month of the taxable year. The due date for the estimated LLC fee is often June 15. Use FTB 3536, *Estimated Fee for LLCs* to make the estimated LLC fee payment.

In addition to California Form 568, the multiple-member LLC which is classified as a partnership for federal tax purposes will report the distributions to its members using the appropriate Schedule Ks:

- Schedule K (568), *Members' Shares of Income, Deductions, Credits, etc.*, is a summary schedule for the LLC's income, deductions, and credits. It represents the combined distributive share items of all the members.
- Schedule K-1 (568), *Member's Share of Income, Deductions, Credits, etc.*, shows each member's distributive share.
- Schedule K-1 (568), column (d): includes the member's distributive share under California law.

- Schedule K-1 (568), column (e): details only income and deductions that are apportioned or sourced to California. For an LLC that is doing business wholly within California, column (e) will generally be the same as column (d), except for nonbusiness income from intangibles. For an LLC doing business within and outside of California, the amounts in column (d) and (e) may be different. The LLC needs to complete Schedule R before completing its member's Schedule K-1, column (e).
- Schedule K-1 (568), Other information line: includes miscellaneous supplemental information necessary at the member level. Supplemental information includes the member's distributive share of:
  - o Aggregate gross receipts, less tax returns and allowances necessary for California Schedule P (540), *Alternative Minimum Tax and Credit Limitations - Residents* and California Schedule P (540NR), *Alternative Minimum Tax and Credit Limitations - Nonresidents or Part-Year Residents*.
  - o Business income and capital gains and losses apportioned to an economic development area.

Estimated Tax for an LLC Classified as a Partnership:

The multiple-member LLC classified as a partnership has no estimated tax requirements. However, California taxes are pay-as-you-go, so partners may have to make estimated tax payments for their own reporting purposes.

- A partner's estimated tax installment payments are due and payable on April 15, June 15, September 15 of the taxable year, and January 15 of the following taxable year.
- Individuals complete California Form 540-ES, *Estimated Tax for Individuals* to report their estimated taxes.
- Generally, you must make estimated tax payments if you expect to owe at least $500 ($250 if married/RDP filing separately) in tax for the current year (after subtracting withholding and credits) and you expect your withholding and credits to be less than the smaller of:
  1. 90 percent of the tax shown on your current tax return; or
  2. 100 percent of the tax shown on your prior year tax return including Alternative Minimum Tax (AMT).
- Each partner is responsible for paying taxes on their distributive share even if they are not actually distributed.

Withholding for an LLC Classified as a Partnership:

General partnerships must withhold 7 percent on distributions of California source income made to domestic nonresident members when distributions to a particular partner exceed $1,500 for the calendar year.

If the multiple-member LLC classified as a partnership pays a nonresident independent contractor for services performed in California, normally, the general partnership must withhold 7 percent on all payments that exceed $1,500 in a calendar year.

If the multiple-member LLC classified as a partnership is required to backup withhold for the Internal Revenue Service, it must also backup withhold for the Franchise Tax Board on California source income. Backup withholding applies to California residents and nonresidents who do not provide a taxpayer identification number or do not certify exemption from backup withholding when required.

The multiple-member LLC which is classified as a partnership for federal tax purposes may be required to withhold taxes if the partnership distributes California source taxable income to a nonresident member.

For more information about withholding, refer to FTB PUB 1017, *Resident and Nonresident Withholding Guidelines*.

LLC Classified as a Corporation

An LLC with either a single member or more than one member can elect to be classified as a corporation rather than be classified as a disregarded entity or partnership under the default rules discussed earlier.

Federal Form 8832 is filed to elect classification as a C corporation.

Federal Form 2553, *Election by a Small Business Corporation*, is filed to elect classification as an S corporation. LLCs electing classification as an S corporation are not required to file Form 8832 to elect classification as a corporation before filing Form 2553. By filing Form 2553, an LLC is deemed to have elected classification as a corporation in addition to the S corporation classification.

Tax Return Filing Guidelines for an LLC Classified as a C Corporation:

- LLCs classified as C corporations that organize in California, register in California, conduct business in California, or receive California source income must file California Form 100, *California Corporation Franchise or Income Tax Return*.
- LLCs must file Form 100 by the 15th day of the 4th month after the close of the taxable year.
- LLCs classified as C corporations are taxed on their net income at a rate of 8.84 percent by California.
- LLCs classified as C corporations are subject to a California minimum tax of $800.
- The California $800 minimum franchise tax is due the first quarter of each accounting period and must be paid whether the corporation is active, inactive, operates at a loss, or files a return for a short period of less than 12 months.
- The California $800 minimum tax is waived on newly formed or qualified LLCs classified as corporations filing an initial return for their first taxable year.

Estimated Tax for an LLC Classified as a C Corporation:

California taxes are pay-as-you-go, so LLCs classified as C corporations may have to make estimated tax payments for their own reporting purposes.

- The LLC's estimated tax is due and payable in four installments on April 15, June 15, September 15, and December 15.
- LLCs classified as C corporations complete and file Form 100-ES, *Corporation Estimated Tax* to report their estimated taxes. (For additional information and applicable rates, go to **ftb.ca.gov/forms** and search for **100-ES**.)
- The California $800 minimum franchise tax is due the first quarter of the LLC classified as a C corporation's accounting period and must be paid whether the LLC is active, inactive, operates at a loss, or files a return for a short period of less than 12 months.

Tax Return Filing Guidelines for an LLC Classified as an S Corporation:

LLCs formed under state civil law may elect to be taxed under the rules of Internal Revenue Code, Subtitle A, Chapter 1, Subchapter S. Corporations taxed following the Subchapter S rules are more commonly known as "S corporations." An entity that has elected to be taxable as an S corporation for federal tax purposes is also treated as an S corporation for California tax purposes. An LLC classified as an S corporation generally offers liability protection to its owners (shareholders) and is a conduit where the profits or losses of the S corporation flow through to the shareholder(s) even if they are not actually distributed. For an LLC created under state law that elects to follow the Subchapter S rules, the members of the LLC are not liable for the losses of the business and creditors may only look to the LLC and its business assets for payment. Other key features of an LLC classified as an S corporation include:

- The number of members may **not** exceed 100.
- Owners may not be partnerships, corporations, or nonresident alien shareholders.
- An LLC classified as an S corporation does not pay federal income tax.
- Under California law, the LLC classified as an S corporation is subject to a 1.5 percent tax on its net income and is a conduit similar to a partnership.
- The items of income, deductions, and credits flow through from the LLC classified as an S corporation to each member through the Schedule K-1(100S), *Shareholder's Share of Income, Deductions, Credits, etc*. Each member is responsible for paying taxes on their pro rata share of the LLC's items of income, deductions, and credits even if they are not actually distributed.

An LLC classified as an S corporation that organizes in California, registers in California, conducts business in California, or receives California source income must file California Form 100S, *California S Corporation Franchise or Income Tax Return.*

The return due date is the 15th day of the 3rd month after the close of the taxable year.

An LLC classified as an S corporation is taxed on its net income at a rate of 1.5 percent for California purposes. LLCs classified as S corporations are not subject to income tax for federal income tax purposes.

LLCs formed under civil law that elect to follow S corporation rules are subject to the annual $800 minimum franchise tax to California. The California $800 minimum tax is waived on newly formed or qualified LLCs filing an initial return for their first taxable year.

The LLC classified as an S corporation must provide each shareholder with a Schedule K-1 (100S) that states the shareholder's pro rata share of the S corporation's items of income, deductions, and credits even if they are not actually distributed.

Estimated Tax for an LLC Classified as an S Corporation:

California taxes are pay-as-you-go, so LLCs classified as S corporations and their members may have to make estimated tax payments for their own reporting purposes.

- LLC's estimated tax is due and payable in four installments on April 15, June 15, September 15, and December 15.
- LLCs complete and file California Form 100-ES, *Corporation Estimated Tax* to report their estimated taxes. (For additional information and applicable rates, go to **ftb.ca.gov/forms** and search for **100-ES**.)
- The California $800 minimum franchise tax is due the first quarter of the LLC's accounting period and must be paid whether the corporation is active, inactive, operates at a loss, or files a return for a short period of less than 12 months.
- An individual member's estimated tax installment payments are due and payable on April 15, June 15, September 15 of the taxable year, and January 15 of the following taxable year.
- Individual members complete California Form 540-ES, *Estimated Tax for Individuals* to report their estimated taxes.
- Generally, you must make estimated tax payments if you expect to owe at least $500 ($250 if married/RDP filing separately) in tax for the current year (after subtracting withholding and credits) and you expect your withholding and credits to be less than the smaller of:
  1. 90 percent of the tax shown on your current tax return; or
  2. 100 percent of the tax shown on your prior year tax return including Alternative Minimum Tax (AMT).

How to End an LLC:

- File California Form 568, Form 100, or Form 100S for the last taxable year, check the box that indicates that it is a final return, and write "Final" on top of the return.
- File California Form 568, Form 100, or Form 100S for all delinquent tax years.
- Pay all outstanding tax liabilities, interest, and penalties.
- Domestic LLCs file the appropriate *Certificate of Dissolution and/or Certificate of Cancellation*, with the California Secretary of State.
- Foreign LLCs file the appropriate *Certificate of Cancellation* with the California Secretary of State.
- Notify all creditors, vendors, suppliers, clients, and employees of your intent to go out of business.
- Close out business checking account and credit cards.
- Cancel any licenses, permits, and fictitious business names.
- Consider publishing a statement in a local newspaper of general circulation near the principal place of business that the limited liability company is no longer in business.
- Refer to FTB PUB 1038, *Guide to Dissolve, Surrender, or Cancel a California Business Entity*, for more information on how to cancel an LLC.

Appendix 1: Doing Business As

Any person or entity carrying on a trade or business for profit in California who decides to use a name which does not include the owner's last name, portray the nature of the business, or is not the entity's legal name, must file a Fictitious Business Name (FBN) statement. This process is also known as registering a "Doing Business As" (DBA) or "Trade Name." The business registers with the Registrar-Recorder/County Clerk's office in the county where the business will be primarily located. If there is no place of business in California, registration is made with the Clerk of Sacramento County.

The filing of a fictitious business name certificate is designed to make available to the public the identities of persons doing business under the fictitious name.

Registration is necessary when:

- A sole proprietorship will be doing business under a name that does not contain the owner's last name.
- A partnership or other association of persons **not** registered with the California Secretary of State (SOS) will use a name that does not include the surname of each general partner or a name that suggests the existence of additional owners such as "Company," "& Company," "& Son," "& Sons," "& Associates," "Brothers," and the like, but not words that merely describe the business conducted.
- A partnership, corporation, or Limited Liability Company (LLC) will be doing business under a name not stated in the articles of incorporation or articles of organization filed with the California SOS.
- The name does not describe the nature of the business.

Example:

If Michael Rocco owns a sole proprietorship, and his business name is Michael Rocco Painting, he won't need a fictitious business name because people will know who the owner of the company is and the type of business. If he wanted to go by either Michael and Sons Painting or House Painting Fast, he would need to file a fictitious business name because the business name suggests additional owners and doesn't include his last name. Likewise, the name Michael Rocco Painting would not be acceptable for a DBA registered to sell real estate. If Michael Rocco instead owned either an LLC or a corporation, and wanted to open up additional businesses under the LLC or corporation, he would need a fictitious business name statement for any business name other than the entity's legal name.

The filing of a FBN, articles of incorporation, or certificate of qualification establishes a rebuttable presumption that the first registrant has the exclusive right to use as a trade name, so long as the name is actually being used.

It is important to select a business name that is not already in use, does not closely resemble an existing business name, or misleads the public. Many cities and counties offer a fictitious business name search on their individual websites. The California Governor's Office of Business and Economic Development conveniently provides links to most county and city websites through its CalGold website, **calgold.ca.gov**. Although a business does not file a fictitious name statement with the Secretary of State, the Secretary of State is a good resource for determining if a business name is already in use.

The fee to file a fictitious business name statement varies depending on the city or county where it is filed. The business owner should direct inquiries to the Registrar-Recorder/County Clerk's office in the county where the business will be primarily located.

The filing is valid for five years or until the facts in the statement change, whichever occurs first.

The business owner usually files a fictitious business name statement within 40 days of starting the business, or before the statement on file expires. Along with the original, the county or city may require several copies of the statement for filing. The clerk or recorder will certify and return all copies to the registrant, keeping the original.

Within 30 days after filing a fictitious business name statement, the registrant must publish the statement in a local newspaper of general circulation near the principal place of business. The notice must appear once a week for four successive weeks. Within 30 days of the last published date, the registrant must file an affidavit of publication with the county or city office. We recommend that you check with the Registrar-Recorder/County Clerk's Office to determine if there is a specific list of approved publications in which to meet this requirement. A business owner should also check with the respective publication when they place the advertisement of the required notice to determine if the publisher will file an affidavit with Registrar-Recorder/County Clerk's Office upon completion.

Appendix 2: Commonly Used Terms

Business License: Business licenses are permits issued by government agencies that allow individuals or companies to conduct business within the government's geographical jurisdiction. It is the authorization to start a business issued by the local government.

Disregarded Entity: A disregarded entity is a business entity that is not recognized as a separate entity for tax purposes. For example, the default rule under the federal "check-the-box" treasury regulations, is that a single member LLC (SMLLC) is considered to be a disregarded entity for tax purposes.

Dissolving, Canceling, or Surrendering an Entity: Business entities doing or transacting business in California or registered with the California Secretary of State (SOS) can dissolve, surrender, or cancel when they cease operations in California and need to terminate their legal existence here. Refer to FTB PUB 1038, *Guide to Dissolve, Surrender or Cancel a California Business Entity*, for more information.

Dividend: A dividend is a sum of money paid regularly (typically quarterly) by a company to its shareholders out of its profits (or reserves).

Doing Business: A taxpayer is doing or transacting business in California if it actively engages in any transaction for the purpose of financial or pecuniary gain or profit in California. For taxable years beginning on or after January 1, 2011, a taxpayer is also doing business in California if any of the following conditions are satisfied:

- A taxpayer is organized or commercially domiciled in California, or
- A taxpayer's California sales, property, or payroll exceed the amounts or percentages then applicable under paragraphs (2), (3), or (4) respectively, of subdivision (b) of California Revenue and Taxation Code section 23101. (Subdivision (d) provides that these amounts include a taxpayer's pro rata or distributive share from pass-through entities.)

More information on this term can be found at **ftb.ca.gov/forms** and FTB PUB 1060, *Guide for Corporations Starting Business in California*.

Fictitious Business Name (FBN): Also known as "Doing Business As" or DBA, a fictitious business name is a business name that is different from your personal name, the names of your partners, or the officially registered name of your LLC or corporation. Refer to Appendix 1 for a more detailed explanation.

Foreign Business Entity: A Business Entity that was formed outside of the state of California or outside of the United States is a foreign business entity. A foreign business entity can qualify/register to transact business in California by filing the applicable form with the California Secretary of State.

Informational Return: An informational return is a tax document or statement that contains information required to be reported to federal and state tax authorities. For example, Federal Forms 1098, and 1099 and California Partnership Return 565 are informational returns.

Pass-through Entity: Pass-through entities are not subject to income tax. Rather, the owners are directly taxed individually on the income, taking into account their share of the profits and losses. Examples include: entities classified as partnerships and entities taxable as S corporations. (However, California also imposes a modified corporate franchise/income tax on S corporations.)

Stock: Stock is a share of a company held by an individual or group. Corporations raise capital by issuing stock and entitle the stock owners (shareholders) to partial ownership of the corporation.

Appendix 3: Quick Reference Chart - Franchise Tax Board Forms of Ownership

The chart below is intended to be for quick reference purposes. The estimated tax dates for C Corportations and S Corporations are based on calendar year operations.

Type	Sole Proprietorship	Partnership		Corporation		Limited Liability Company		
		General	**Limited**	**C Corporation**	**S Corporation**	**Disregarded Single Member/ Partnership**	**C Corporation**	**S Corporation**
Tax Forms	540	565		100	100S	568	100	100S
Due Dates	April 15	15th Day of the 3rd Month		15th Day of the 4th Month	15th Day of the 3rd Month	15th Day of the 3rd Month	15th Day of the 4th Month	15th Day of the 3rd Month
Tax Rate	1%-13.3%	N/A		8.84%	1.50%	N/A	8.84%	1.50%
Taxed On	Total Taxable Income	Distributive Shares (K-1s)		Net Income	Net Income	Total California Sourced Income	Net Income	Net Income
Minimum Franchise Tax	N/A	N/A	N/A	$800	$800	N/A	$800	$800
Annual Franchise Tax	N/A	N/A	$800	N/A	N/A	$800	N/A	N/A
Estimated Tax Form	540-ES	N/A	N/A	100-ES	100-ES	N/A	100-ES	100-ES
Estimated Due Date	April 15	Reported on Personal Income Tax Return by each Partner		April 15		Reported on Personal Income Tax Return by Single Member and by each Partner	April 15	
	June 15			June 15			June 15	
	September 15			September 15			September 15	
	January 15			December 15			December 15	

Go to **ftb.ca.gov** for information about less common forms of ownership such as a Limited Liability Partnership (LLP), Limited Liability Limited Partnership (LLLP), and Series Limited Liability Company (Series LLC). More helpful information for California businesses including DBAs is also available at the California Business Portal at **businessportal.ca.gov** and GO-Biz at **business.ca.gov.**

For Additional Information:

ftb.ca.gov

800.852.5711

For General Information:

taxes.ca.gov

STATE OF CALIFORNIA
Franchise Tax Board

FTB 1123 (REV 11-2016)