



Summary Analysis of Amended Bill

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Sponsor:

Bill Number: AB 364

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Amended: April 29, 2019

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Related Bills: See Prior Analysis

Subject: Limited Partnerships and Limited Liability Companies Annual Tax Exemption

Summary

This bill would, under the Personal Income Tax Law (PITL), exempt new Limited Partnerships (LPs) and new Limited Liability Companies (LLCs) that are small businesses, from the payment of the annual tax for their first taxable year.

This analysis only addresses the provisions of the bill that impact the department's programs and operations.

Recommendation – No position.

Summary of Amendments

The April 29, 2019, amendments made technical changes, added a sunset date, and added Revenue and Taxation Code (R&TC) section 41 requirements.

As a result of the amendments, the department's technical considerations discussed in the department's analysis of the bill as introduced February 4, 2019, were resolved. Except for the "Effective/Operative Date," "This Bill," and "Economic Impact" sections, the remainder of the department's analysis of the bill as introduced February 4, 2019, still applies. For convenience, "Implementation Considerations," "Fiscal Impact," and "Policy Concerns" sections are stated below.

Effective/Operative Date

As a tax levy, this bill would be effective immediately upon enactment and specifically operative for taxable years beginning on or after January 1, 2020, and before January 1, 2025.

This Bill

For taxable years beginning on or after January 1, 2020, and before January 1, 2025, this bill would create an exemption from the annual tax for the first taxable year for an LP or LLC that is a new, small business doing business in this state or organized or registered to conduct business in this state, and required to file a return under Sections 18633 or 18633.5.

The exemption would be inapplicable to an LP or LLC that reorganizes solely for the purpose of reducing its annual tax, or fails to file a timely return.

For purposes of the exemption, this bill would define the following terms:

- “New limited partnership” means an LP that is formed on or after January 1, 2020, except for an LP that either:
 - Began business operations as, or acquired its business operations from, a sole proprietorship, an Limited Liability Partnership (LLP), or any other form of business entity prior to beginning business operations, or
 - Acquired its business operations from an LP.
- “New limited liability company” means an LLC that is formed on or after January 1, 2020, except for an LLC that either:
 - Began business operations as, or acquired its business operations from, a sole proprietorship, an LLP, or any other form of business entity prior to beginning business operations,
 - Acquired its business operations from an LLC.
- “Small business” means an LP or LLC that has “gross receipts, less returns and allowances, reportable to this state,” for the taxable year, of \$50,000 or less.
- “Gross receipts, less returns and allowances, reportable to this state” means the sum of the gross receipts from the production of business income, as defined in subdivision (a) of Section 25120,¹ and the gross receipts from the production of nonbusiness income, as defined in subdivision (d) of Section 25120.²

This bill states that it is the intent of the Legislature to apply the requirements of R&TC section 41. This bill would require the Legislature to collect data to determine if the annual tax exemption is meeting, failing to meet, or exceeding the goals as stated in the bill.

This credit would be repealed by its own terms on December 1, 2025.

¹ “Business income” means income arising from transactions and activity in the regular course of the taxpayer’s trade or business and includes income from tangible and intangible property if the acquisition, management, and disposition of the property constitute integral parts of the taxpayer’s regular trade or business operations.

² “Nonbusiness income” means all income other than business income.

Implementation Considerations

The department has identified the following implementation concern. Department staff is available to work with the author's office to resolve these and other concerns that may be identified.

Because the bill fails to specify otherwise, a return filed by the extended due date by an otherwise eligible LP or LLC would be considered timely filed and eligible for the exemption. If this is contrary to the author's intent, the bill should be amended.

Fiscal Impact

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

Economic Impact

Revenue Estimate

This bill would result in the following revenue loss:

Estimated Revenue Impact of AB364 as Amended April 29, 2019
Assumed Enactment after June 30, 2019

(\$ in Millions)

Fiscal Year	Revenue
2019-2020	-\$19
2020-2021	-\$32
2021-2022	-\$33

This analysis does not account for changes in employment, personal income, or gross state product that could result from this bill or for the net final payment method of accrual.

Revenue Discussion

Based on Franchise Tax Board income data for LPs and LLCs for the 2015 taxable year, it is estimated that in the 2020 taxable year there would be approximately 1,300 first year LPs and 38,000 first year LLCs with gross receipts of \$50,000 or less that would be subject to the annual tax under current law and would benefit from the first year annual tax exemption. This would result in an estimated revenue loss of \$32 million in the 2020 taxable year.

The tax year estimates are converted to fiscal year estimates, and then rounded to arrive at the amounts reflected in the above table.

Policy Concerns

This bill would provide a tax benefit for LPs, and LLCs subject to the PITL, that would not be provided to LLPs. Thus, this bill would provide differing tax treatment to taxpayers based solely on their classification or form of organization.

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