



## **Bill Analysis**

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Sponsor: Three-Member  
Franchise Tax Board

Phone: (916) 845-2551

Bill Number: SB 934

Introduced: February 6, 2020

## **SUBJECT**

Eliminate the tax-exempt application fee and the Form 199 filing fee

## **SUMMARY**

This bill, under the Corporation Tax Law (CTL), would eliminate the fee for submission of a tax-exempt application and the annual information return filing fee applicable to exempt organizations, and would update cross-references under the Health and Safety Code and the Vehicle Code.

## **RECOMMENDATION**

Support.

On December 07, 2017, the three-member Franchise Tax Board voted 2-0, with Member Ortega, representative of the Department of Finance abstaining, to sponsor this language.

## **SUMMARY OF AMENDMENTS**

None noted.

## **REASON FOR THE BILL**

The reason for this bill is to simplify the processing of tax-exempt applications by eliminating an outdated and unnecessary application fee as well as providing equitable and fair tax treatment for similarly-situated entities by eliminating an annual information fee required only for exempt organizations.

## **ANALYSIS**

This bill, under the CTL, would eliminate both the twenty-five dollar (\$25) fee for submission of a tax-exempt application and the ten dollar (\$10) annual information return filing fee applicable to exempt organizations.

### *Effective/Operative Date*

This bill would be effective and operative on January 1, 2021.

### *Federal/State Law*

#### Tax-Exempt Application

The Internal Revenue Service (IRS) charges a user fee for the submission of the federal application for tax exemption. The amount of the user fee for an organization that files a 1023-EZ, is \$275. Generally, for other organizations that are exempt under Internal Revenue Code (IRC) section 501 or 521 that do not file a 1023-EZ, the fee is \$600.

California law treats federally tax-exempt IRC section 501(c)(3), 501(c)(4), 501(c)(5), 501(c)(6), 501(c)(7), or 501(c)(19) organizations as tax-exempt under state income tax law if the organization submits form FTB 3500A, Submission of Exemption Request, and a copy of its federal determination letter to the Franchise Tax Board (FTB)(see Appendix A for further detail). No filing fee is required. If the organization does not meet the above requirements and applies for California tax exempt status, the FTB is required to charge a twenty-five dollar (\$25) filing fee with the application for exemption (form FTB 3500).

#### Annual Information Filing Return

Current federal law requires a tax-exempt organization to file an annual information return or notice with the IRS, unless an exception applies, and no filing fee is assessed. If an organization fails to file for three consecutive years, it will lose its federal tax-exempt status (IRC section 6033(j)).

Current state law provides that an organization that is required to file an annual information return (Form 199) shall pay a filing fee of ten dollars (\$10). Failure to pay the filing fee timely results in an increase of the filing fee to twenty-five dollars (\$25).

### *Implementation Considerations*

Implementing this bill would require changes to existing tax forms and instructions, the business entity accounting system, and web content that could be accomplished during the normal annual update.

### *Technical Considerations*

None noted.

### *Policy Concerns*

None noted.

## LEGISLATIVE HISTORY

AB 94 (Rodriguez & Cervantes, Chapter 104, Statutes of 2017) allows federally tax-exempt veterans' organizations under IRC section 501(c)(19) to use the streamlined method of applying for tax-exemption for state purposes.

AB 1173 (Bocanegra, Chapter 536, Statutes of 2013) allows an organization that has obtained a ruling or determination from the IRS that it is exempt from federal income taxes as an organization described in Section 501(c)(3), (c)(4), (c)(5), (c)(6), or (c)(7) of the IRC to use the streamlined method of applying for tax-exemption for state purposes.

AB 1677 (Nestande, Chapter 858, Statutes of 2012) increased the general filing-requirement threshold of the California exempt organization annual information return from \$25,000 of average annual gross receipts to \$50,000 of such receipts.

AB 404 (Eng, Chapter 504, Statutes of 2009) eliminated the requirements for certain tax-exempt entities that are granted a federal group exemption to apply separately for state tax exemption, and allowed the FTB to permit inspection of certain exemption documents.

## PROGRAM BACKGROUND

### *Tax-Exempt Application Fee*

Since January 1, 1970, a filing fee of twenty-five dollars (\$25) is required to be submitted with a tax-exempt application to reimburse the state's general fund for the FTB costs to process the application. In 2013, state law enacted the simplified method that allowed certain types of federal tax-exempt organizations to obtain state exempt status with no fee. In addition to the simplified filings, the FTB receives approximately 5700 tax-exempt applications a year, a few fail to include the application fee, requiring additional correspondence and tracking. The twenty-five dollar (\$25) fee paid with the tax-exempt application is not captured in, or cost effective to add to, FTB's automated accounting systems and must be manually tracked. General fund recovery fees require additional manual processing to credit the payments appropriately, which increases the department's costs to process the payments.

### *Annual Information Filing Return (Form 199) Fee*

Certain tax-exempt nonprofit organizations are required to file an annual information return and pay a ten dollar (\$10) filing fee, due with regard to an extension. Existing law provides specified exemptions from this filing requirement, including an exemption for smaller organizations with normal annual gross receipts of less than \$50,000. Rather than filing the two-page information return, these exempt organizations submit basic information electronically using a California e-Postcard (Form 199-N) and are relieved from paying the ten dollar (\$10) filing fee. With the exception of corporations

expecting a net operating loss carryback and the Form 199 filing fee, all other state franchise and income tax returns require the tax to be paid by the original due date of the return, without regard to any extension. Additionally, tax-exempt organizations are the only entities required to pay a fee for filing an annual information return.

**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 SB 934 as Introduced February 6, 2020  
Assumed Enactment after June 30, 2020

<b>Fiscal Year</b>	<b>Revenue</b>
2020-2021	-\$600,000
2021-2022	-\$900,000
2022-2023	-\$900,000

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

*Revenue Discussion*

This estimate includes both the impact from eliminating the \$25 filing fee submitted with form FTB 3500 and the \$10 fee submitted with FTB Form 199.

**Eliminate the Form FTB 3500 Exempt Application Fee**

In fiscal year 2018-2019, the FTB received approximately 5,700 tax-exempt application forms. Based on the average growth over the previous four years, form volumes are expected to be approximately 6,000 in fiscal year 2020-21. Because the bill is operative beginning January 1, 2021, half-way through the 2020-2021 fiscal year, the estimated net revenue loss from the elimination of the application fee would be approximately \$75,000 in fiscal year 2020-2021 and increase to \$150,000 in fiscal year 2021-2022.

*Eliminate the FTB Form 199 Filing Fee*

In tax year 2017, the FTB received \$800,000 in filing fees and penalties from approximately 60,000 entities that filed Form 199. The estimated revenue loss from the elimination of the filing fee would be approximately \$800,000 in the 2021 and 2022 taxable years.

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

**LEGAL IMPACT**

None noted.

**APPOINTMENTS**

None noted.

**SUPPORT/OPPOSITION**

Support: On December 07, 2017, the three-member Franchise Tax Board voted 2-0, with Member Ortega, representative of the Department of Finance abstaining, to sponsor this language.

Opposition: None noted.

**ARGUMENTS**

To be determined.

**LEGISLATIVE STAFF CONTACT**

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## Appendix A

### Explanation of Exempt Code Sections of the IRC

IRC Section	Organization
501(c)(3)	Religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals
501(c)(4)	Civic leagues or organizations
501(c)(5)	Labor, agricultural, or horticultural organizations
501(c)(6)	Business leagues, chambers of commerce, real-estate boards, boards of trade, or professional football leagues
501(c)(7)	Clubs organized for pleasure, recreation, and other nonprofitable purposes
501(c)(19)	Veterans' organizations