



## Bill Analysis

Author: Bigelow

Sponsor:

Bill Number: AB 664

Related Bills: See Legislative  
History

Introduced February 12, 2021

## SUBJECT

Suspend Annual & Minimum Franchise Tax for Small Businesses during COVID State of Emergency

## SUMMARY

This bill, under the Personal Income Tax Law (PITL), would suspend the due date for payment of the annual tax for limited partnerships (LPs), limited liability partnerships (LLPs), and limited liability companies (LLCs) not classified as corporations, that are small businesses as defined in the Government Code (GC), until the end of the state of emergency declared by the Governor on March 4, 2020.

This bill would also suspend the accrual of penalties or interest related to the payment of the annual tax for those taxable years for small businesses.

## RECOMMENDATION

No position.

## SUMMARY OF AMENDMENTS

Not applicable.

## REASON FOR THE BILL

The reason for this bill is to provide tax relief for certain small businesses in California until the COVID-19 state of emergency has ended.

## ANALYSIS

For taxable years beginning on or after January 1, 2020, this bill, under the PITL, would suspend the requirement to pay the annual tax for LPs, LLPs and LLCs not classified as corporations, which are small businesses until the end of the state of emergency declared by the Governor on March 4, 2020.

This bill would define the term “small business” under Section 14837 of the GC. For purposes of this bill, “small business” means either:

1. An independently owned and operated business that is not dominant in its field of operation, the principal office of which is located in California, the officers of which are domiciled in California, and which, together with affiliates, has 100 or fewer employees, and average annual gross receipts of fifteen million dollars (\$15,000,000) or less over the previous three years.
2. A manufacturer that is primarily engaged in the chemical or mechanical transformation of raw materials or processed substances into new products, is classified between Codes 31 to 33, inclusive, of the North American Industry Classification System, and has 100 or fewer employees.

This bill would also add that penalties or interest related to the payment of the annual tax for those taxable years would not accrue until the state of emergency declared by the Governor on March 4, 2020, related to the COVID-19 virus ends.

#### *Effective/Operative Date*

This bill would be effective immediately and retroactively operative for taxable years beginning on or after January 1, 2020.

#### *Federal/State Law*

##### *Federal Law*

Federal law does not require payment of an annual tax for LPs, LLPs, and LLCs.

##### *State Law*

In general, LPs, LLPs, and LLCs not classified as corporations are subject to an annual tax equal to the \$800 minimum corporate franchise tax.

The annual tax is due and payable for LLCs on the 15<sup>th</sup> day of the fourth month after the beginning of the current tax year (generally April 15 of the current year for calendar year taxpayers.) The annual tax for LPs and LLPs is due on the original due date of the return, the 15<sup>th</sup> day of the third month following the close of its year (generally March 15 of the year following the tax year for calendar year taxpayers.

LPs, LLCs, and registered LLPs or foreign LLPs that did no business in California during taxable year that is 15 days or less are not subject to the tax for that first short year.

In addition, every LP, LLP, and LLC not classified as a corporation that organizes, registers, or files with the California Secretary of State on or after January 1, 2021, and before January 1, 2024, is exempt from the annual tax for its first taxable year.

### *Implementation Considerations*

Department staff has identified the following implementation considerations for purposes of a high-level discussion; additional concerns may be identified as the bill moves through the legislative process. Department staff is available to work with the author's office to resolve these and other concerns that may be identified.

This bill was introduced in the 2021 legislative session and would make the annual tax paid for taxable year 2020 not due until after the state of emergency ends. This would allow taxpayers to claim refunds for annual tax already paid for taxable years beginning on or after January 1, 2020. The taxpayers would also receive interest on these refunds. If this is contrary to the author's intent, the bill could be amended not to allow refunds of amounts already paid.

In addition, the department has already developed the forms and instructions for the 2020 taxable year and collected annual taxes that are currently due with returns filed for the 2020 taxable year. Thus, the department may incur additional costs to develop additional tax forms and instructions necessary to implement this retroactive provision. To alleviate these concerns, the author may wish to change the operative date to January 1, 2022.

Under Revenue and Taxation Code (RTC) section 41, legislation that would create a new tax expenditure, which includes a credit, deduction, exclusion, exemption, or any other tax benefit as provided for by the state, is required to include specific goals, purposes, objectives, and performance measures to allow the Legislature to evaluate the effectiveness of the tax benefit. This bill should be amended to satisfy the RTC section 41 requirements.

### *Technical Considerations*

Section 19001.5 of this bill incorrectly references Part 11, the tax on corporations, not Part 10, which contains the annual tax on LPs, LLPs, and LLCs classified as partnerships. For consistency with other sections, the following changes are recommended:

Notwithstanding Section 19001, for taxable years beginning on or after January 1, 2020, for every taxpayer that is a small business, as that term is defined by Section 14837 of the Government Code, payment of the tax imposed under Part ~~11~~ 10 (commencing with Section ~~23001~~ 17001) shall not be due, and penalties or interest related to the payment of the tax for those taxable years shall not accrue, until the state of emergency declared by the Governor on March 4, 2020, related to the COVID-19 virus, has ended.

### *Policy Considerations*

This bill intends to provide a tax benefit for small businesses under the CTL and PITL. However, this bill would provide a tax benefit for LPs, LLPs, and LLCs classified as partnerships, under the PITL that would not be provided to other business entities such as corporations. Thus, this bill would provide differing treatment to small businesses based solely on classification.

Although this bill provides for a suspension of the LLC annual tax, LLCs that are small businesses would still be subject to the LCC fee. If that is not the intent of the author, the language will need to be amended.

### **LEGISLATIVE HISTORY**

AB 85 (Committee on Budget, Chapter 8, Statutes of 2020), under the PITL, provided a first year exemption from the annual tax for LPs, LLPs, and LLCs not classified as corporations.

AB 308 (Muratsuchi, Chapter 421, Statutes of 2019), under the PITL and the CTL, allowed an exemption from the annual tax or the minimum franchise tax for certain small business LLCs and corporations that are solely owned by a deployed member of the U.S. Armed Forces, and the LLC or corporation operates at a loss or ceases to operate, for taxable years beginning on or after January 1, 2020.

AB 250 (Choi, 2019/2020) would have, under the CTL, modified the minimum franchise tax for corporations having less than \$15 million in gross receipts, and under the PITL, would have retained the \$800 minimum annual tax. AB 250 did not pass out of the Assembly by the constitutional deadline.

AB 2306 (Melendez, 2019/2020) would have, under the CTL, repeal the \$800 corporate minimum franchise tax for corporations doing business in the state for taxable years beginning on or after January 1, 2020. AB 2306 did not pass out of the Assembly Revenue and Taxation Committee by the constitutional deadline.

AB 2929 (Arambula and Muratsuchi, 2019/2020) would have, under the PITL and the CTL, reduce the annual tax for certain single-member LLCs and the minimum franchise tax for certain single-owner corporations to provide that these taxpayers would not be subject to the tax in their first taxable year, and for the following four years, the tax would incrementally increase annually by two hundred dollars (\$200); with a limitation of minimum tax reduction of one hundred million dollars (\$100,000,000) per taxable year and annual tax reduction of one hundred million dollars (\$100,000,000) per taxable year, administered by the FTB on a first-come-first-served basis. AB 2929 did not pass out of the Assembly Revenue and Taxation Committee by the constitutional deadline.

SB 349 (Portantino, 2019/2020), under the PITL and the CTL, would have modified the minimum franchise tax for corporations having less than \$15 million in gross receipts and would have allowed an exemption from the annual tax or the minimum franchise tax for certain small business LLCs and corporations that were solely owned by a deployed member of the U.S. Armed Forces. SB 349 was vetoed by the governor whose veto message stated in part, "The intent of this bill is to provide tax relief for smaller California businesses and to encourage economic growth. Both are important goals which I support, and helping small businesses is certainly a priority I share with the Legislature. However, this bill would be better addressed through the annual budget process."

### **PROGRAM BACKGROUND**

None noted.

### **FISCAL IMPACT**

This bill would impact the department's systems, resulting in programming and processing revisions. The department's costs to implement this bill have yet to be determined. As the bill continues to move through the legislative process, costs will be identified.

### **ECONOMIC IMPACT**

#### *Revenue Estimate*

This bill would suspend the due date for payment of the annual tax and the accrual of penalties or interest related to the payment of the annual tax for LPs, LLPs, and LLCs that are small businesses not classified as corporations. The suspension would remain in place until the end of the state of emergency declared by the Governor. It is estimated the total tax impact would be no more than \$500,000.

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.

### **LEGAL IMPACT**

None noted.

### **APPOINTMENTS**

None noted.

### **SUPPORT/OPPOSITION**

To be determined.

**ARGUMENTS**

To be determined.

**LEGISLATIVE CONTACT**

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