



Bill Analysis

Author: Valladares

Sponsor:

Bill Number: AB 91

Related Bills: See Legislative
History

Amended: January 3, 2022

SUBJECT

Reduced Annual Tax and Minimum Franchise Tax for Small Businesses and Microbusinesses

SUMMARY

This bill, under the Personal Income Tax Law (PITL), would reduce the annual tax for limited partnerships (LPs), limited liability partnerships (LLPs), and limited liability companies (LLCs) not classified as corporations, that are small businesses or microbusinesses, as defined, from \$800 to \$400 or \$200, respectively. In addition, under the Corporation Tax Law (CTL), this bill would reduce the minimum franchise tax for corporations that are small businesses or microbusinesses, as defined, from \$800 to \$400 or \$200, respectively.

RECOMMENDATION

No position.

SUMMARY OF AMENDMENTS

The January 3, 2022, amendments changed the operative dates, added sunset dates, replaced Section 41 intent language with specific goals and a performance indicator, added a Franchise Tax Board (FTB) reporting requirement, and made other nonsubstantive changes. The considerations discussed in the department's analysis of the bill as introduced December 7, 2020, continue to apply, and another implementation consideration has been identified.

REASON FOR THE BILL

The reason for this bill is to provide relief to California's struggling small businesses by reducing the \$800 annual tax and minimum franchise tax to \$400 for small businesses and to \$200 for microbusinesses.

ANALYSIS

For taxable years beginning on or after January 1, 2022, and before January 1, 2027, this bill would reduce the annual tax and minimum franchise tax for certain entities that are organized, qualified to conduct business, or doing business in the state.

This bill, under the PITL, would reduce the annual tax for LPs, LLPs, and LLCs not classified as corporations, which are small businesses, as defined, from \$800 to \$400, and that are microbusinesses, as defined, from \$800 to \$200.

In addition, this bill, under the CTL, would reduce the minimum franchise tax for corporations that are small businesses, as defined, from \$800 to \$400, and that are microbusinesses, as defined, from \$800 to \$200.

This bill states that "small business" and "microbusiness" have the same meaning as those terms defined under Government Code (GC) section 14837. For purposes of this bill:

A "small business" means either:

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 \$15,000,000 or less over the previous three years.

Or is a manufacturer with 100 or fewer employees.

A "microbusiness" is either:

A small business which, together with affiliates, has average annual gross receipts of \$5,000,000 or less over the previous three years.

Or is a manufacturer with 25 or fewer employees.

A "manufacturer" means a business that meets both of the following requirements, it is:

Primarily engaged in the chemical or mechanical transformation of raw materials or processed substances into new products.

Classified between Codes 31 to 33, inclusive, of the North American Industry Classification System.

The bill provides that the goal, purpose, or objective of the bill is to relieve the financial burden for small and microbusinesses in California, and that the performance indicator for the Legislature to use when measuring whether the bill meets this goal is the number of registered small businesses and microbusinesses in California.

In accordance with GC section 9795, Reports to the Legislature, the FTB, on or before January 1, 2028, must provide the Assembly Revenue and Taxation Committee and the Senate Governance and Finance Committee a report detailing the number of small businesses and microbusinesses in California subject to the minimum franchise tax.

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, 2022, and before January 1, 2027.

Federal/State Law

Federal Law

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

State Law

Unless specifically exempted by statute, every corporation or LLC classified as a corporation that is organized, qualified to conduct business, or doing business in this state (whether organized in-state or out-of-state), is subject to the minimum franchise tax of \$800.

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

Every corporation that incorporates or qualifies to conduct business in this state on or after January 1, 2000, is exempt from the minimum franchise tax for its first taxable year. This exemption is inapplicable to a corporation that reorganizes solely for the purpose of avoiding payment of its minimum franchise tax.

For taxable years beginning on or after January 1, 2020, an LLC or corporation that is a small business solely owned by a deployed member of the United States (U.S.) Armed Forces is not subject to the annual tax or minimum franchise tax for any taxable year that the owner is deployed and the LLC or corporation operates at a loss or ceases operation.

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, and is available to work with the author's office to resolve this and other concerns that may be identified.

The bill's definition of a "small business," "microbusiness," or "manufacturer," pursuant to GC 14837, refers to the term "gross receipts." Typically, thresholds for income tax purposes use the term "gross income" to allow FTB to more easily perform validation, if needed. For clarity, and consistency within the RTC, it is recommended that the bill be amended to refer to "gross income."

SEC. 5 of the bill was amended to require the FTB to provide a report containing certain data on the utilization of this credit by January 1, 2028. However, the department generally does not collect the specified data and, in addition, would not have the data by the required reporting date. The author may wish to amend the bill to resolve these considerations by making these suggested revisions:

SEC. 5.

(a)(2) The performance indicator for the Legislature to use when measuring whether the amendments meet the goal, purpose, or objective specified in paragraph (1) is the ~~number of registered small and microbusinesses in California.~~ *annual data, as reported by taxpayers to the Franchise Tax Board, on the number of tax returns reporting the reduced minimum tax, and the average amount of tax reported by those who benefit from the reduced minimum tax.*

(b) On or before ~~January~~*October* 1, 2028, the Franchise Tax Board shall provide a report to the Assembly Revenue and Taxation Committee and the Senate Governance and Finance Committee on the number of small and microbusinesses in California *that benefited from the reduced* ~~subject to the~~ minimum franchise tax. The report shall be provided in compliance with Section 9795 of the Government Code.

Technical Considerations

For clarity that exceptions, such as the first taxable year exception and small business solely owned by a deployed member of the U.S. Armed Forces exception, do apply before application of this bill, the following changes are recommended:

17935 (g) (1) Except as otherwise provided *in subdivision (f)*, for taxable years beginning on or after January 1, 2021, a limited partnership shall pay to the state an annual tax of:

(A) If the limited partnership is a small business, \$400.

(B) If the limited partnership is a microbusiness, \$200.

17941 (h) (1) Except as otherwise provided *in subdivisions (f) and (g)*, for taxable years beginning on or after January 1, 2021, a limited liability company shall pay to the state an annual tax of:

(A) If the limited liability company is a small business, \$400.

(B) If the limited liability company is a microbusiness, \$200.

17948 (f) (1) Except as otherwise provided [in subdivision \(e\)](#), for taxable years beginning on or after January 1, 2021, a limited liability partnership shall pay to the state an annual tax of:

(A) If the limited liability partnership is a small business, \$400.

(B) If the limited liability partnership is a microbusiness, \$200.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

AB 632 (Ramos, 2021/2022), under the CTL, would reduce the \$800 minimum franchise tax for corporations, and, by reference, the annual tax for LPs, LLPs, or LLCs not classified as corporations, based on gross receipts. AB 632 did not pass out of the Assembly Revenue and Taxation Committee by the constitutional deadline.

AB 664 (Bigelow, 2021/2022), under the PITL, would suspend the due date for payment of the annual tax for LPs, LLPs, and LLCs not classified as corporations, that are small businesses, until the end of the state of emergency declared by the Governor on March 4, 2020. AB 664 did not pass out of the Assembly Revenue and Taxation Committee by the constitutional deadline.

AB 806 (Chen, et al., 2021/2022) would, under the PITL, exempt LPs, LLPs, and LLCs not classified as corporations from the payment of the annual tax for taxable years beginning on or after January 1, 2020, and before January 1, 2023. In addition, this bill would, under the CTL, exempt corporations from the payment of minimum franchise tax for taxable years beginning on or after January 1, 2020, and before January 1, 2023. AB 806 did not pass out of the Assembly Revenue and Taxation Committee by the constitutional deadline.

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 \$15,000,000 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, 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, 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 \$200; with a limitation of minimum tax reduction of \$100,000,000 per taxable year and annual tax reduction of \$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 \$15,000,000 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 result in the following revenue loss:

Estimated Revenue Impact of AB 91 as Amended January 3, 2022
Assumed Enactment after June 30, 2022

(\$ in Millions)

Fiscal Year	Revenue
2022-2023	-\$600
2023-2024	-\$550
2024-2025	-\$500

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

The Assembly Revenue and Taxation Committee analysis of AB 91, dated January 7, 2022, lists the following support and opposition.

Support

California Society of Enrolled Agents
Howard Jarvis Taxpayers Association

Opposition

California Teachers Association

ARGUMENTS

None noted.

LEGISLATIVE CONTACT

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