

ALERT

California Expands First-Year Exemption From Minimum Franchise Tax

Limited liability companies (“LLCs”), limited partnerships (“LPs”) and limited liability partnerships (“LLPs”) that are registered to do business in California are currently required to pay an annual franchise tax of Eight Hundred Dollars (\$800) to the state’s Franchise Tax Board (the “FTB”). California corporations have long been exempt from the minimum franchise tax for their first year of existence. However, this exemption did not extend to LLCs, LPs or LLPs.

California has now extended the first-year exemption to LLCs, LPs and LLPs. In order to relieve pandemic-related financial pressures for newly formed businesses, and to encourage the registration of new businesses, Governor Gavin Newsom extended the first-year exemption to LLCs, LPs and LLPs, as part of the 2020 Budget Act. Any LLC, LP or LLP that registers or files with the California Secretary of State on or after January 1, 2021 and before January 1, 2024, is exempt from paying the Eight Hundred Dollar (\$800) minimum tax in its first taxable year. The purpose of this change is to remove a barrier to small business creation, particularly for new businesses that are still operating at a loss or have limited income in their first year.

Starting in their second taxable year, all LLCs, LPs, LLPs, and corporations that are organized in California or qualified to do business in California become subject to the annual Eight Hundred Dollars (\$800) annual minimum franchise tax, until they formally dissolve. Additionally, LLCs, LPs and LLPs that have gross income of more than Two Hundred Fifty Thousand Dollars (\$250,000) in their first year, will continue to be required to pay a gross receipts tax, beginning at Nine Hundred Dollars (\$900) and up to Eleven Thousand Seven Hundred Ninety Dollars (\$11,790). Corporations, as well as LPs and LLPs, are not subject to the gross receipts tax.

The FTB plans to review annual reports from the Franchise Tax Board for the next several years and evaluate whether the new law does indeed increase the number of LLCs, LPs and LLPs that form in California.

If you have questions or would like further information regarding tax obligations applicable to California businesses, please do not hesitate to contact us.



Author

[Lindsey A. Harms](#)
T 925.944.9700
lharms@brothersmithlaw.com

BROTHERS SMITH LLP provides its clients, professional advisors and its friends with up-to-date reports on recent developments in business, real estate, employment, estate planning and taxation.

CIRCULAR 230 DISCLOSURE – Pursuant to rules and regulations imposed by the Internal Revenue Service, any tax advice contained in this communication, including any attachments, is not intended or written to be used, and cannot be used, for the purpose of (1) avoiding tax penalties under the Internal Revenue Code or (2) promoting, marketing or recommending to another person any transaction or matter addressed herein.

The summary which appears above is reprinted for information purposes only. It is not intended to be and should not be considered legal advice nor substitute for obtaining legal advice from competent, independent, legal counsel. If you would like to discuss these matters in more detail, please feel free to contact us so that we can provide the clarification and resources you need to make effective decisions.



2033 North Main Street, Suite 720
Walnut Creek, California 94596
T 925.944.9700 F 925.944.9701

www.brothersmithlaw.com

