



STATE OF CALIFORNIA  
**Franchise Tax Board**

# **Commercial Cannabis Activity: Personal Income Tax Law – Business Expenses Report**

**Economic and Statistical Research Bureau**

## **Purpose**

This report is intended to fulfill the Franchise Tax Board's obligation under Assembly Bill 37 (Chapter 792, Statutes of 2019) which added Revenue and Taxation Code Section 17209 and included language that the Franchise Tax Board shall annually report to the Legislature by July 31, the number and total dollar amount of deductions and credits claimed under this section for the most recent calendar year in which either the deductions or credits are allowed.

Prepared by the Staff of the  
Franchise Tax Board  
STATE OF CALIFORNIA

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## **Background**

In 2016, Proposition 64 was approved by California voters. This proposition legalized commercial adult-use of cannabis and imposed two specific taxes on cannabis, an excise tax to be paid by consumers and a stepped cultivation tax to be paid by growers/cultivators.

In 2022, Assembly Bill 195 (Chapter 56, Statutes of 2022) passed the High-Road Cannabis Tax Credit and the Cannabis Equity Tax Credit. In addition, the bill repealed the cultivation tax as of July 1, 2022. For the newly created credits, the bill requires the Franchise Tax Board (FTB) to begin reporting in March of 2025. To learn more about these credits please visit the FTB's website.

The intent of this law is to provide tax equity to the cannabis industry and allow commercial cannabis licensees, reporting under the Personal Income Tax code, to claim deductions and credits available to other legal businesses in the state.

Under federal law (Internal Revenue Code (IRC) section 280E), taxpayers in the cannabis industry may not deduct business expenses or claim credits for activities related to a controlled substance. With the adoption of Proposition 64 and the subsequent passage of Assembly Bill 37 (Chapter 792, Statutes of 2019), California Personal Income Tax Law (PITL) allowed sole proprietorships and partnerships to claim credits and deductions for business expenses paid or incurred during the taxable year in carrying on commercial cannabis activity. This provision of California law is operative for taxable years beginning on or after January 1, 2020, and before January 1, 2025.

## **Franchise Tax Board Statutory Reporting Requirements**

Under Chapter 792 of the Statutes of 2019 (AB 37), the FTB is required to provide an annual report to the Legislature, on or before July 31, in which either the deductions or credits are allowed. The FTB shall have the following reporting requirements:

- The number of deductions and credits claimed pursuant to Section 17209 of the Revenue and Taxation Code (RTC).
- The total dollar amount of deductions and credits claimed pursuant to Section 17209 of the RTC.

## **Data**

Beginning on or after January 1, 2020, California allows taxpayers operating under the PITL to claim credits and deduction of business expenses paid or incurred during the taxable year in conducting commercial cannabis activity (under RTC section 17209).

Because there is no reliable method of identifying qualified taxpayers, such as a cannabis Principal Business Activity code, the FTB created the information reporting form, FTB 4197, to capture the performance metrics identified by the Legislature as required for this report. When taxpayers file the FTB 4197, they voluntarily self-report the business information needed, however the form is not required to be filed to claim qualified deductions and credits nor is there a penalty for failing to file form FTB 4197. Additionally, because many cannabis businesses are formed as partnerships, the business income and expenses flow-through to members or shareholders, and the business activities are reported by taxpayers on their personal income tax returns. These personal income taxpayers may not have the information necessary to file and report deductions and credits allowed under RTC Section 17209.

Table 1 presents data based on form 4197 data processed as of March of 2024 for credits and deductions allowed for business expenses paid or incurred for tax years 2021 through 2023. The data is based on taxpayer's self-reported tax return information.

**Table 1: Total Credits and Deductions Allowed by Tax Year\*\***

Tax Year	Number of Returns	Total Credits Allowed	Total Deductions Allowed
2021	55	\$10,644	\$248,987
2022*	N/A	N/A	N/A
2023*	N/A	N/A	N/A

\*The number of 2022 and 2023 tax year returns reporting data on cannabis activities is too small to be reported under state taxpayer privacy rules. Additionally, not all timely 2023 tax year returns have been processed as of this writing.

\*\* Form 4197 data processed through March of 2024.

Although we believe more taxpayers are claiming the credits and deductions allowed under Chapter 792, Statutes of 2019 (AB 37), the information processed to date continues to show very few of these forms have been filed. Based on available data, the number of returns and the amount of deductions and credits claimed on the 2022 and 2023 tax year returns cannot be disclosed due to state privacy rules. The FTB will continue to undertake efforts to improve taxpayer awareness of the existence, purpose, and correct usage of form 4197.

Please visit FTB's website for income tax information on the [Cannabis Industry](#).