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State of California  
**Franchise Tax Board**

04.14.2008

**FTB NOTICE – 2008-2**

**SUBJECT: Processing Limited Liability Company Fee Claims for Refund as a Result of *Northwest Energetic Services, LLC v. Franchise Tax Board* (2008) 159 Cal.App. 4<sup>th</sup> 841**

**Purpose:** To inform Limited Liability Companies (LLCs) that filed claims for refund that additional information is required to determine if their circumstances are identical to those involved in *Northwest Energetic Services, LLC v. Franchise Tax Board*<sup>1</sup> (*Northwest*), so that their claims for refund may be acted upon.

In addition, this notice will inform LLCs that operate in a manner similar to *Northwest* that now wish to file claims, assuming the statute of limitations remains open, of the information that should be included with the claim in order for it to be promptly processed.

**Background:** In *Northwest* the Court of Appeal held that the LLC fee imposed pursuant to former California Revenue and Taxation Code (CR&TC) section 17942 was unconstitutional as applied to *Northwest* because the fee was calculated by reference to the total income of an LLC that conducted no business in California. The decision of the Court of Appeal in *Northwest* is final as to the constitutional issue,<sup>2</sup> so that refunds of the LLC fee assessed for taxpayers that are similarly situated to *Northwest* may commence. Note that the Court of Appeal's decision did not hold that the LLC fee statute was unconstitutional "on its face"; rather, it held that the LLC fee statute was unconstitutional "as applied" to *Northwest*. Therefore, the *Northwest* decision addresses only circumstances where a taxpayer has no income from activities in California. It does not address the circumstances where an LLC earns income from activities only in California or earns income from activities both within and without California. Those circumstances are being addressed in separate cases.

**The Limited Liability Company Fee Prior to January 1, 2007**

Prior to the enactment of Assembly Bill 198 (Stats. 2007, Ch. 381, effective on October 10, 2007, and operative for taxable years beginning on or after January 1, 2007), LLCs paid an annual fee based on the LLC's total income from all sources reportable to this state. The LLC fee was in addition to the annual tax set forth in CR&TC section 17941. Former CR&TC section 17942, subdivision (b)(1), defined total income as "gross income, as defined in Section 24271, plus the cost of goods sold that are paid or incurred in connection with the trade or business of the taxpayer." Therefore, an LLC doing business wholly outside of California was required to pay the LLC fee based on its worldwide total income, regardless of the fact it had no income attributable to activities in California.

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<sup>1</sup> *Northwest Energetic Services, LLC v. Franchise Tax Board* (2008) 159 Cal.App. 4<sup>th</sup> 841, mod. (Mar. 3, 2008), petn. for review pending with respect to attorney fees.

<sup>2</sup> The Franchise Tax Board has appealed the attorney fees portion of the decision.

## **The Limited Liability Company Fee Beginning On or After January 1, 2007**

After the enactment of Assembly Bill 198, CR&TC Section 17942 was revised. The LLC fee is now determined by reference to the total income derived from or attributable to California. The total income attributable to California is determined by utilizing the sales factor rules contained in CR&TC sections 25135 and 25136 (as modified by the regulations under CR&TC section 25137, if applicable). The regulations under CR&TC section 25137 that exclude receipts from the sales factor entirely are not applied in any case.

## **The LLC Fee Litigation**

Three separate cases have been filed challenging the constitutionality of the LLC fee. Each case presents separate circumstances and each is in a different status.

***Northwest Energetic Services, LLC v. Franchise Tax Board*** – The LLC in this case registered with the Secretary of State but did no business in California. The Court of Appeal held that assessing an LLC fee on an entity that had no income attributable to activities in California was unconstitutional and the fee should be refunded. That case is now final with respect to the constitutional issue.

***Ventas Finance I, LLC v. Franchise Tax Board***, Court of Appeal, First Appellate District, A116277, A117751 - The LLC in this case had income attributable to activities within and without California. The case has been fully briefed and is pending the scheduling of oral argument. There is no final decision in the case.

***Bakersfield Mall, LLC v. Franchise Tax Board***, San Francisco Superior Court CGC-07-462728 - The LLC in this case alleges it conducted all of its activities in California. The case is ongoing.

## **Claims for Refund Previously Filed**

The Franchise Tax Board received a number of claims for refund from LLCs based upon the above cases. Action on these claims was deferred pending the outcomes of the LLC fee litigation described above. Because the decision in *Northwest* with respect to the LLC fee is now final, action can be taken on claims for LLCs that have the same facts as were involved in that case (i.e., an LLC that conducted no activities in California). Because claims were filed before the completion of the litigation, some claims contained insufficient information to determine whether the LLC that filed the claim has the same facts as those involved in *Northwest*.

If you filed a claim with facts that are similar to those involved in *Northwest*, you must provide the following additional information:

1. **The LLC's name and address, including the name and phone number of the managing member or designated contact person.**
2. **The LLC's Secretary of State file number or Franchise Tax Board temporary LLC number (for unregistered entities) and Federal Employer Identification Number.**
3. **Taxable year(s) involved**
4. **A statement that the LLC did no business in California for each of the taxable years for which the claim is being filed.**

This information may be faxed to the Franchise Tax Board at:

**(916) 845-9796**

Or this information may be mailed to:

**ABS 389 MS: F340  
Franchise Tax Board  
P.O. Box 942867  
Sacramento, CA 94267-8888**

For Courier Service Delivery or Private Courier Mail:

**ABS 389 MS: F340  
Franchise Tax Board  
C/O FTB Notice 2008-2  
Sacramento, CA 95827**

Faxed information will expedite the receipt of your information and processing of your claim.

Supplying this information will enable FTB to process claims based on the *Northwest* decision without delay. Without this additional information being provided, claimants may need to wait until all of the pending cases involving the LLC fee have been decided to receive their refund. If it appears from the information the department already possesses that the LLC had activity within California, the claim will not be acted upon until the other cases involving the LLC fee have been decided and are final.

### **New Claims for Refund**

If an LLC wants to file a protective claim based on the *Northwest* decision, the LLC or its representative should fax a letter to the Franchise Tax Board stating "This letter constitutes a protective claim for refund for (taxpayer's name). - No Income Attributable to California." The letter must include the amount of the fee for which a refund is claimed for each year and it must provide the information listed above in items 1-4 under "claims for refund previously filed." Fax this letter to the same fax number or mail addresses shown above. The LLC's managing member or representative with a power-of-attorney must sign this letter, under penalty of perjury.

The principal author of this notice is Benjamin F. Miller of the Franchise Tax Board, Legal Division. For further information regarding this notice, contact Ms. Colleen Berwick at P.O. Box 1720, Rancho Cordova, CA 95741-1720.