



BDO Seidman, LLP
Accountants and Consultants

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Subject:
Update –
California Limited
Liability Company
(LLC) Fee Status

State Tax Alert

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For more information about the Court decision and potentially filing protective refund claims on behalf of affected companies, please contact:

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Earlier this year, a California Superior Court ruled in *Northwest Energetic Services LLC v. California Franchise Tax Board* (“Northwest”) that the California LLC fee was a tax and as such was unconstitutional because it applied to all LLCs that were organized or legally qualified to do business in California, even if the LLC did not have any business activities in the state. Additionally, the LLC fee was computed on the total income of the LLC even if it operated in other states. This decision was subsequently appealed by the California Franchise Tax Board (“FTB”) to the California Supreme Court which has agreed to hear the case. On November 7, 2006, a California Superior Court released another tentative decision in favor of an LLC that was actually doing business in California and in other states, *Ventas Finance I, LLC v. FTB (“Ventas”)*. This decision reiterated the earlier Northwest decision where it was ruled that the LLC fee was an unconstitutional tax. It is likely that the FTB will appeal this decision and that both cases will be heard jointly by the California Supreme Court.

Recommended Action

The statute of limitations for refunds in California is generally the later of four years from the date of filing a return or one year from the date of overpayment. Therefore, if an LLC meets the protective refund claim profile as listed below, it should be analyzing all LLC returns filed with California within the last four years for potentially filing protective refund claims.

As the FTB appealed the Northwest decision and will likely do so with the Ventas decision as well, we are recommending the filing of “Protective Refund Claims” for those LLCs meeting the criteria listed below. It is recommended that current year originally filed California LLC returns should still compute the LLC fee on total income since the FTB will still apply the law related to the computation of the fee and may impose penalties and interest related to the underpayment.

Protective Refund Claim Profile

LLCs that are classified as partnerships or disregarded entities for federal income tax purposes that filed a California LLC Return of Income (Form 568) within the past four years (i.e., after November 15, 2002) and paid the LLC fee.