

California Nonprofit Law Essentials, Part 4: State Tax Exemption

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Federal recognition is only half the story. In California, an IRS letter doesn't automatically mean you have state tax exemption.

When California nonprofits think about "tax exemption," they usually picture the IRS determination letter. But securing federal tax exemption is only half the story. To be fully recognized as exempt in California, an organization must also take steps at the state level.

That means filing with the **Franchise Tax Board (FTB)** and, in certain cases, with other state or county agencies. Without these additional approvals, a nonprofit may find itself unexpectedly subject to state income, property, or sales taxes.

Federal Recognition Isn't Enough

An IRS determination letter is an important milestone, but in California it doesn't automatically exempt a nonprofit from state-level corporate franchise and income taxes. The Franchise Tax Board requires its own review before granting recognition.

Until the FTB issues a determination letter, a nonprofit may still be treated as taxable in California — even if it is fully exempt at the federal level. In other words, federal recognition is necessary, but not sufficient, for complete exemption.

Applying for State Exemption



California nonprofits have two possible filing paths, and the choice can significantly affect how quickly exemption is secured.

The first option is **Form 3500A**, a short application available to organizations already recognized under section 501(c)(3) by the IRS. It may look like the faster route, but in practice it can cause long delays. Because Form 3500A cannot be filed until after the IRS determination letter is received — a process that often takes 12–18 months — nonprofits can end up waiting nearly two years before their California exemption is finalized.

The second option is **Form 3500**, the state's full exemption application. It requires more documentation — Articles of Incorporation, bylaws, program descriptions, and budgets — but it can be filed right away, without waiting for the IRS. And current FTB processing times for Form 3500 are often shorter than those for Form 3500A.

That's why at FPLG, we prepare the full Form 3500 for our clients. It avoids unnecessary delays, provides a clear state determination of exemption earlier in the process, and allows founders to move forward with confidence while their federal exemption is still pending.

Property and Sales Tax Relief

State-level recognition by the FTB primarily addresses California's income and franchise taxes. But nonprofits may also qualify for additional relief at the property and sales tax level.

The most significant benefit is the **Welfare Exemption from property tax**. Charitable nonprofits that own real or personal property, and use it exclusively for exempt purposes, may apply for this exemption. The process is not automatic: it requires filing paperwork with the county assessor's office, which then coordinates with the FTB to verify eligibility. The exemption can provide substantial savings for organizations that own office buildings, program facilities, or even equipment used in their charitable work.

There are also some limited opportunities for relief from **sales and use taxes**. Some nonprofits may qualify to avoid paying sales tax on certain purchases directly related to their charitable activities. Others may be allowed to hold occasional sales — such as fundraising auctions, raffles, or events — without collecting or remitting sales tax. These exemptions are narrower, require careful analysis of eligibility, and must be requested through the **California Department of Tax and Fee Administration (CDTFA)**.

Together, these additional exemptions can significantly reduce a nonprofit's operating costs. But, like income tax exemption, they require deliberate applications and ongoing compliance to maintain.

Staying Compliant with the FTB

Receiving your FTB determination letter is not the end of the story. Just like the IRS, the state expects nonprofits to remain compliant on an ongoing basis.

Every California nonprofit with state tax exemption must file an annual return. Larger organizations typically file **Form 199 (Exempt Organization Annual Information Return)**, while smaller nonprofits — those with gross receipts under \$50,000 — may file the simplified **Form 199N (the "e-postcard")**.



These filings are due even if your nonprofit had little or no activity during the year.

In addition to annual filings, nonprofits must keep their organizing documents and activities aligned with exempt purposes. If you amend your Articles of Incorporation or bylaws, or if your nonprofit significantly changes its programs, you may need to notify the FTB. And if you receive any notices or inquiries from the FTB, timely response is essential.

Failing to meet these obligations can lead to penalties, suspension of corporate status, or even revocation of exemption. In the worst-case scenario, the organization could be taxed as a regular corporation, undermining its mission and credibility.

The Bottom Line

For California nonprofits, securing tax exemption is a **two-step process**: first at the federal level with the IRS, and then at the state level with the Franchise Tax Board. A federal determination letter alone is not enough.

Once state recognition is secured, nonprofits may also explore valuable opportunities for property and sales tax relief. But exemption is not a one-time event — it carries annual reporting and compliance responsibilities that must be taken seriously.

By staying current with the FTB and other agencies, your organization can minimize its tax burden and keep more resources devoted to mission-driven work.

Coming next in the [California Nonprofit Law Essentials](#) series: the role of the **board of directors** — fiduciary duties, meetings, and governance practices under California law.