

DELAWARE CORPORATE FRANCHISE TAX:

ARE YOU PAYING TOO MUCH?

All corporations legally incorporated under the laws of Delaware are required to file an Annual Corporate Franchise Tax Report and pay a franchise tax. The minimum tax is \$35 and the maximum tax is \$165,000. Corporations may be overpaying this tax because it is more similar to an annual fee than a tax, and many corporations just pay the tax as assessed. Corporations receive an invoice from the Delaware Department of State (“Department”), and generally pay the invoice amount as stated. However, there is an alternative method to calculate the tax at the corporation’s discretion that may provide tax savings. Additionally, with some legal planning, a corporation may also be able to minimize its annual tax.

Actions to Minimize the Tax

Some basic steps to consider in attempting to properly calculate and minimize the Franchise Tax include:

1. Calculate the tax utilizing the Assumed Par Value Method
2. Evaluate the business purpose for the amount of authorized shares
3. Determine that you are using the correct tax base if utilizing the alternative Assumed Par Value Method
4. Properly account for any changes in the corporation’s capital structure during the previous tax year
5. Evaluate the use of intercompany debt versus capital contributions
6. Was the corporation inactive during the privilege period?

The Basics of the Tax

The Annual Corporate Franchise Tax Report (and tax invoice, which are the same document) is generally mailed to the corporation’s Delaware registered agent in December. Taxes and annual reports must be filed and received by the Department no later than March 1 of each year. Corporations should note that the “timely mailed, timely filed” standard for most income tax returns is not the standard for the Franchise Tax. The report and tax must actually be in the hands of the Department no later than March 1. Interest and penalties are imposed if the return and tax are received after March 1.

Also, corporations whose tax liability is more than \$5,000 are required to make quarterly estimates. The amount of the estimate and the due dates are as follows: the first installment of 40% is due June 1; the second installment of 20% is due by September 1; the third installment of 20% is due by December 1; and the fourth and final installment is due when filing the annual report on or before March 1.

The Department calculates a corporation’s tax liability under the Authorized Shares Method, which is based upon the number of the corporation’s authorized shares legally on record with the Department, and issues a tax invoice to the corporation. The tax is \$35 for 3,000 or less authorized shares, \$62.50 for 3,001 - 5,000 authorized shares, \$112.50 for 5,001 - 10,000 authorized shares, and \$112.50 + \$62.50 for

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STATE & LOCAL TAX PERSPECTIVE

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each 10,000 or fraction thereof of above 10,000 authorized shares. For example, if the corporation has 10,000 authorized shares, the default tax is \$112.50, but it is \$175.00 for 10,001 shares.

In addition to the default Authorized Shares Method, each corporation may elect to calculate its tax based upon the alternative Assumed Par Value Method. The election is made simply by making some notations on the annual report and submitting the recalculated tax. The Assumed Par Value Method determines a par value for each authorized share based upon the value of Total Assets / Issued Shares. The corporation's total assumed par value is divided by 1,000,000 and then multiplied by \$250 to determine the tax.

Stevens & Lee's State Local Tax Practice has extensive experience evaluating Delaware corporate franchise tax liabilities. In conjunction with our Firm's corporate practice, we can help you determine whether there is an opportunity to develop and execute a plan to minimize your corporation's Delaware Franchise Tax.

For more information about Stevens & Lee's State and Local Tax Practice, please visit our website at www.stevenslee.com/practice/salt.htm. Tom Bowen and Matt Wilk together have over 25 years of state and local tax experience. Contact them directly at:

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