
SENATE COMMITTEE ON REVENUE AND TAXATION

Senator Jerry McNerney, Chair
2025 - 2026 Regular

Bill No: AB 1675

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Consultant: Grinnell

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Tax Levy: Yes

Fiscal: Yes

CORPORATION TAX LAW: TAX EXPENDITURES: NO TAX BREAKS FOR ICE CONTRACTORS ACT OF 2026

Enacts the No Tax Breaks for ICE Contractors Act of 2026.

Background

Businesses can be organized in many different forms by filing specified documents with the Secretary of State. Once formed, for-profit businesses incur state income tax obligations. How California taxes a business depends largely on the entity's form. Specifically:

- Businesses formed as C-corporations are subject to California's Corporation Tax, and generally taxed on their net income or profit at the entity level. A corporation's owners or shareholders also incur a tax liability on their personal income tax returns when the corporation pays a dividend, or when they generate a capital gain from the sale of stock.
- Other business types are taxed as pass-through entities, where income tax is usually not applied at the entity level, but rather the income of the business is "passed through" to owners who report the income from the business on their personal income tax returns and are subject to the Personal Income Tax. Pass-through entities (PTEs) include S-corporations, Limited Liability Companies (LLCs), partnerships, and disregarded-entity pass-throughs (single-owner entities) such as sole proprietorships, single-member LLCs, and qualified Subchapter S subsidiaries. However, in some cases, these entities may elect to be taxed as corporations. California also imposes entity-level taxes on most PTEs under the Personal Income Tax.

Corporate income tax. While some states apply taxes on a business's gross receipts, California taxes net apportioned *business* income and allocated net *nonbusiness* income of corporations doing business in California at a rate of 8.84%, or imposes the \$800 minimum tax, whichever is greater. California applies the combined report method for corporate taxation. This method requires a corporation computing its California tax liability to include the tax returns of each of its unitary subsidiaries and affiliates into one report. The combined report method generally allows for the cancellation of any intercompany transactions, such as dividends paid from a subsidiary to its corporate parent. However, taxpaying corporations can elect to exclude the income and expenses of its foreign subsidiaries from its combined report, called the "water's edge" election, with some exceptions.

Tax expenditures. California law allows various income tax credits, deductions, exemptions, and exclusions. The Legislature enacts such tax incentives to compensate taxpayers for incurring certain expenses, such as child adoption, or to influence certain behavior, such as charitable

giving. The Legislature uses tax incentives to encourage taxpayers to do something they would otherwise not do, but for the tax credit. The Department of Finance (DOF) is required to annually publish a list of tax expenditures, which currently total around \$94.2 billion per year.¹

Tax credits. Among its tax expenditures, California currently offers several credits against Personal Income and Corporation Taxes to create incentives for certain behavior, including:

- The California Competes Tax Credit
- California Motion Picture and Television Production Tax Credit, including the Soundstage Filming Tax Credit
- Cannabis Equity Credit
- College Access Tax Credit
- Disabled Access for Eligible Small Business
- Donated Fresh Fruits and Vegetables
- High-Road Cannabis Employer
- Homeless Hiring Credit
- Low-Income Housing Tax Credit
- Natural Heritage Preservation
- New Advanced Strategic Aircraft
- New Employment Credit
- Prior Year Alternative Minimum Tax Credit
- Prison Inmate Labor
- Research and Development
- State Historic Preservation Credit

Credit Limitation. In 2024, the Legislature limited the total of all business credits, with some exceptions, including credit carry forwards, to \$5,000,000 in the 2024, 2025, and 2026 taxable years, unless the Director of Finance determines that General Fund money over the multiyear forecast is sufficient *without* the revenue impact of the net operating loss suspension and credit limitation (SB 167 and SB 175, Committee on Budget & Fiscal Review). Taxpayers can make an irrevocable election to receive an annual refundable credit claimed in future tax years for business credits equal to credit amounts not claimed due to the limitation.

In his 2026-27 May Revision to the Governor's Budget, Governor Newsom proposed to permanently limit tax credit use to \$5 million or 50% of liability, whichever is greater, effective in the 2027 taxable year and thereafter. This week, the Legislature approved SB 122 (Committee on Budget & Fiscal Review), which extends the current temporary limitation while maintaining the refundable credit election until the 2030 taxable year, with some modifications, after which time credits are limited to 75% of liability or \$5 million, whichever is greater.

Immigration Enforcement. Beginning in January 2025, Immigration and Customs Enforcement (ICE) launched an interior enforcement campaign with no parallel in recent history in both its scale and its tactics. According to the Brookings Institution, federal immigration policy previously worked through the criminal justice system and remained largely out of public view, and a person generally had to be arrested for something unrelated to their immigration

¹ <https://dof.ca.gov/media/docs/forecasting/revenue-and-taxation/tax-expenditure-reports/2025-26-Tax-Expenditure-Report.pdf>

status before ICE decided whether to begin removal proceedings.² Agents conducted worksite raids, entered private homes, and made arrests outside schools, churches, and hospitals. Of the 115,000 arrests ICE made in the first half of 2025, 55,000 were at large, meaning they took place in the community, rather than in jails or detention facilities. Videos of these encounters spread widely on social media, and news coverage was extensive and sustained.

The Brookings reports adds:

The consequences of arrest are serious and well-publicized. Detainees report overcrowded, freezing conditions. At least 46 people died in detention. ICE transferred individuals to a maximum-security prison in El Salvador and sent others to South Sudan. Family members have been unable to locate detained relatives. Though unauthorized immigrants were most at risk, legal status offered unreliable protection. ICE deported Kilmar Ábrego García despite a standing court order barring his removal, a case that drew national attention but was not isolated. Additionally, current policy creates a “chilling effect”, whereby immigrant households, including those with legal status, withdrew from public life out of fear of interacting with government officials.

Seeking to eliminate tax subsidies for companies that have increasingly profited from mass immigration detention, the author wants to make companies contacting with the Department of Homeland Security ineligible for state tax credits.

Proposed Law

Assembly Bill 1675 enacts the No Tax Breaks for ICE Contractors Act of 2026, which makes ineligible for a credit against the Corporation Tax for the taxable year any contracting corporation, defined as one that contracts with the Department of Homeland Security, either directly or through subcontracts, to provide goods or services through the federal government procurement or contracting process that does not include goods or services acquired through a platform or mechanism available to the general public. The bill applies to contracts with the “Department of Homeland Security” when the Department of Homeland Security is contracting on behalf of either the United States Customs and Border Protection or the United States Immigration and Customs Enforcement, as well as contracts with the United States Customs and Border Protection, United States Immigration and Customs Enforcement, and the Management Directorate.

The bill exempts from its provisions tax credits received by any direct or indirect partner or member of a nonprofit sponsored venture to which the claiming party has made a direct or indirect loan or capital contribution, as well as Low-Income Housing Tax Credits directly or indirectly purchased from a nonprofit housing sponsor.

The bill requires the Franchise Tax Board (FTB) by June 1, 2027, to estimate the amount of revenue that would have resulted if the modifications made by the bill, with respect to the eligibility for tax credits, applied to the 2026 taxable year, and notify the Controller of that amount. Each June 1st thereafter, the measure directs FTB to estimate the amount of revenue

² Marcela Escobari, Ian Seyel, and Paul Beach. “Shock, awe, and economic fallout: The employment effects of ICE enforcement in US cities.” *Brookings*. May 29, 2026. <https://www.brookings.edu/articles/ice-enforcement-employment-effects-us-cities/>

resulting from the bill's provisions in the previous year and notify the Controller. The bill then directs the Controller to transfer an amount equal to the amounts in those notifications from the General Fund to the California Immigrant Resilience Fund, which the bill establishes in the State Treasury. The Legislature can then appropriate moneys in the Fund for grants or contracts, *and* state operations, under the authority of a program administered by the State Department of Social Services, to contract with qualified nonprofit legal services organizations to provide legal services to unaccompanied undocumented minors who are transferred to the care and custody of the federal Office of Refugee Resettlement and who are present in this state, for the sole purpose of providing legal representation to unaccompanied undocumented minors who are in the physical custody of the federal Office of Refugee Resettlement or who are residing with a family member or other sponsor.

AB 1675 provides that the Administrative Procedures Act does not apply to any standard, criterion, procedure, determination, rule, notice, guideline, or any other guidance it establishes or issues, and sunsets its provisions on December 1, 2032.

State Revenue Impact

According to FTB, "To determine the magnitude of the potential revenue impact of this bill, the number of business entities no longer eligible for tax credits and the amount of tax credits that would no longer be available to those businesses must be known. Because it is difficult to predict the number of affected business entities that would be ineligible for any tax credits and the amount of disallowed tax credits, the revenue impact of this bill is unknown. However, it is assumed that for every \$1 million in tax credits claimed by qualified taxpayers who would become ineligible under this bill, the estimated revenue gain would be \$1 million."

Comments

1. **Purpose of the bill.** According to the author, "ICE is executing Americans, abducting toddlers, and violently breaking into homes and cars to drag innocent people into their unmarked vehicles. More kidnappings mean more profits for ICE contractors. By doing business with armed and masked thugs acting with impunity, corporations are raking in multi-million deals and tearing families apart. ICE must be abolished and its rogue elements prosecuted. The No Tax Breaks for ICE Contractors Act ensures that California does not subsidize corporations that profit off of ICE's terror campaign, and instead directs public investments to our communities."
2. **Precedents.** The Legislature has enacted several tax incentives over the years to encourage taxpayers to do something they would otherwise not do, but for the tax credit. While the Legislature has limited the utilization of tax credits for all taxpayers to generate revenue (and may do so again soon), and denied business expense deductions for clubs that restrict membership or the use of its services or facilities on the basis of ancestry, it hasn't limited a taxpayer's ability to claim credits because it disfavors its otherwise lawful business activities. Additionally, proceeds of the state's general taxes – Personal Income, Corporation, and Sales and Use – flow to the General Fund, from which the Legislature appropriates them in the Budget Act. AB 1675 would instead allocate its revenues outside the Budget Act to the California Immigrant Resilience Fund, only allowing the Legislature to then appropriate those funds for purposes of immigration-related services and programs within the state. The Legislature can appropriate any funds it wishes for those purposes by appropriation or the Budget Act. Lastly, the measure also isn't clear whether its additional revenues are subject to Proposition 98's K-14 educational

guarantee or whether Proposition 2's Budget reserve must be satisfied before the Controller transfers moneys from the General Fund to the California Immigrant Resilience Fund.

3. Proportionality. AB 1675 applies to any contract with an entity that contracts with the Department of Homeland Security, either directly or through subcontracts, to provide goods or services. Its credit limitation applies regardless of the number or duration of the contracts, or the type of goods or services contracted for. As a result, firms that provide goods and services that directly support mass deportation are treated in the same way as a company that provides products and services necessary to facility operation, like food service, janitorial supplies, or health care.

4. Self-reporting. AB 1675 would have each of the 1.1 million annual Corporation Tax filers answer a question on the return whether they meet the criteria set by the bill, making them ineligible to claim a tax credit. If they answer "No", they can claim a credit, but if they answer "Yes," FTB must deny any claimed credit. As a result, the bill's effectiveness will largely depend on truthful voluntary self-reporting and auditing efforts. While taxpayers are subject to a penalty of perjury when filing a return, criminal convictions are rare. If FTB were to go beyond the taxpayer's answer for the question on the return, an audit would require inspecting a company's contracts to determine whether the entities they contract with met the criteria in the bill, which would differ from FTB's current audit process that mainly seeks to verify that the amount of tax paid is accurate.

5. Loopholes. Large companies can have thousands, if not tens of thousands, of subsidiaries and affiliates. Two or more corporations conducting a unitary business within and outside of California must use the combined reporting approach to determine California source income. However, AB 1675 applies to individual corporate taxpayers, not combined groups. As a result, a corporation taxpayer with tax credits that would be ineligible to claim them, because it is invested in or contracts with an entity defined in AB 1675, could simply assign them to another company within its combined group using current law (AB 1452, Committee on Budget, 2008). The taxpayer receiving the credit could simply claim the credit assigned to it to reduce its tax, therefore leaving the combined group no worse off as a result of the bill. Additionally, because the measure only applies to the Corporation Tax, a firm could reorganize as an S-Corporation of Limited Liability Company and evade the bill's provisions entirely because those entities are taxable under the Personal Income Tax.

6. Implementation. AB 1675 requires FTB to estimate the amount of revenue that would have resulted if the modifications made with respect to the eligibility for tax credits made by the bill applied to the 2026 taxable year and notify the Controller of that amount by June 1, 2027. However, the filing deadline for business entities for the 2026 taxable year was March 2027, with many filing a six-month extension. It will take time for FTB to scan and process returns, as well as make an estimate, which is unlikely to be completed in time. Additionally, the bill does not contain language aligning each of the annual taxable year estimates required by the bill with the Controller's transfers.

7. Not everything. As noted above, AB 1675 applies solely to credits against the Corporation Tax, and not the Personal Income Tax. Additionally, the measure would not apply to the California Alternative Energy and Advanced Transportation Financing Authority's (CAEATFA's) sales and use tax exclusion program, which awards state and local sales and use tax exemptions to successful applicants who are manufacturers of alternative source technology

used for renewable electricity generation, advanced transportation, advanced manufacturing, and that use recycled feedstock.

8. Related legislation. At its June 24th hearing, the Committee will also consider:

- AB 1633 (Haney), which imposes an annual tax upon all “private detention facility operators” equal to 50% of the operator’s gross receipts derived from the operation of each “private detention facility” in California.
- AB 2465 (Ortega), which makes a business entity ineligible for any credit under the Personal Income or Corporation Taxes if it is directly invested in, owns, manages, or profits from a private detention facility, or contracts with a private detention facility or agency engaging in immigration enforcement.

9. 2/3. AB 1675 constitutes a change in state statute that would result in any taxpayer paying a higher tax, which requires a 2/3 vote by each house of the Legislature to be enacted under Section 3 of Article XIII A of the California Constitution.

Assembly Actions

Assembly Judiciary Committee:	9-3
Assembly Revenue & Taxation Committee:	5-2
Assembly Appropriations Committee:	11-4
Assembly Floor:	55-20

Support and Opposition (6/18/26)

Support: California Community Foundation
 California Federation of Teachers
 Drug Policy Alliance
 Los Angeles County Democratic Party
 Santa Monica Democratic Club
 Western Center on Law & Poverty, Inc.

Opposition: Acclamation Insurance Management Services
 Allied Managed Care
 American Petroleum and Convenience Store Association
 Associated General Contractors - San Diego Chapter
 Associated General Contractors, California
 CalBroadband
 California Association of Sheet Metal & Air Conditioning Contractors National Association
 California Bankers Association
 California Chamber of Commerce
 California Chapters of the National Electrical Contractors Association
 California Legislative Conference of Plumbing, Heating & Piping Industry
 California Taxpayers Association
 California Trucking Association
 Construction Employers’ Association
 Flasher Barricade Association

National Electrical Contractors Association
Screen Credits, LLC
Southern California Contractors Association
United Contractors
Wall and Ceiling Alliance
Western Wall and Ceiling Contractors Association

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