

Date of Hearing: April 13, 2026

ASSEMBLY COMMITTEE ON REVENUE AND TAXATION
Mike Gipson, Chair

AB 2084 (Bauer-Kahan) – As Amended March 27, 2026

Majority vote. Tax levy. Fiscal committee.

SUBJECT: Corporation Tax Law: tax-exempt organizations: revocation of tax-exempt status

SUMMARY: Provides the Franchise Tax Board (FTB) with the discretion to retain an organization's tax-exempt status for state income tax purposes if it determines the organization's suspension or revocation of federal tax-exempt status was not for reasons specified by existing federal law and regulations. Specifically, **this bill:**

- 1) Authorizes the FTB, in its discretion, to retain an organization's tax-exempt status for state income tax purposes if it determines that the suspension or revocation of its tax-exempt status for federal tax purposes is not related to any of the following:
 - a) Fraud or intentional misrepresentation;
 - b) Misuse or diversion of organizational funds;
 - c) Failure to file necessary returns or reports; or,
 - d) Other significant breaches of organizational reporting or governance requirements.
- 2) Authorizes the FTB to prescribe any regulations or procedures necessary to implement the evaluation process described above.
- 3) Takes immediate effect as a tax levy.

EXISTING LAW:

- 1) Exempts the income of various types of nonprofit organizations from corporation taxes. (Internal Revenue Code (IRC) Section 501(c) and Revenue and Taxation Code (R&TC) Section 23701.)
- 2) Exempts from taxation nonprofit organizations that are organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals, provided that no part of the net earnings inures to the benefit of any private shareholder or individual and no substantial part of its activities involve lobbying or political campaigning. (IRC Section 501(c)(3) and R&TC Section 23701d.)
- 3) Prohibits senior officials of the United States executive branch, including the president, from requesting, either directly or indirectly, that the Internal Revenue Service (IRS) conduct or

cease an audit or other investigation of any taxpayer (including tax-exempt entities). Any officer or employee of the IRS receiving any such request shall report it to the Treasury Inspector General for Tax Administration. (IRC Section 7217.)

- 4) Requires nonprofit organizations to submit an application to the FTB to obtain California tax-exempt status and requires the FTB to review the application and issue a determination. This application is referred to as FTB Form 3500. (R&TC Section 23701(a).)
- 5) Provides a streamlined method for specified nonprofit organizations that have obtained a ruling, determination, or specified letter from the IRS regarding the organization's federal tax-exempt status to obtain state tax-exempt status by attaching their federal determination letter to their application to the FTB. This application is referred to as FTB Form 3500A. (R&TC Section 23701(a).)
- 6) Requires a nonprofit organization whose federal tax-exempt status is suspended or revoked to notify the FTB of the suspension or revocation if they received state tax-exempt status through the streamlined method based on their federal determination. (R&TC Section 23701(b)(3).)
- 7) Requires the FTB, upon notification that an organization's federal tax-exempt status was suspended or revoked, to suspend or revoke the organization's tax-exempt status for California income tax law purposes. (R&TC Section 23701(b)(3).)
- 8) Provides that these provisions shall not be construed to prevent the FTB from revoking the exemption of an organization that is not organized or operated in accordance with California law or IRC Sections 501(c)(3), 501(c)(4), 501(c)(5), 501(c)(6), 501(c)(7), or 501(c)(19). (R&TC Sections 23701a, 23701d, 23701e, 23701f, 23701g, and 23701w.)

FISCAL EFFECT: The FTB estimates that, for every \$1 million of income that will no longer be exempted from state taxation, the revenue increase to the state would be approximately \$90,000. As such, Committee staff estimates the fiscal effect to exceed this Committee's Suspense File threshold.

COMMENTS:

- 1) The author has provided the following statement in support of this bill:

Nonprofit organizations play a vital role in serving communities and advancing charitable, educational, and public-interest missions. Recent federal rhetoric and actions have raised serious concerns about the potential for abrupt challenges to nonprofit tax-exempt status when organizations are perceived by the federal administration to be acting outside their exempt purposes rather than genuine compliance issues.

AB 2084 authorizes the California Franchise Tax Board to preserve a nonprofit's state income-tax exempt status when a federal revocation occurs for reasons unrelated to legal eligibility for revocation. AB 2084 ensures that legitimate organizations are not immediately stripped of their status due to administrative issues or evolving federal interpretations. AB 2084 promotes fairness and stability for nonprofits while preserving the state's ability to enforce compliance with tax-exempt requirements.

- 2) This bill is sponsored by the California Association of Nonprofits, which notes, in part:

Since it became available in 2008, the FTB Form 3500A has enabled many California nonprofits to pursue their state tax-exempt status based on their existing federal 501(c)(3) determination. This welcome efficiency creates what has become a precarious dependency: if the federal government revokes an organization's 501(c)(3) status, potentially as a targeting tactic against programmatic work deemed politically unfavorable, California is statutorily required to revoke that organization's state exemption as well. The FTB currently lacks the authority to delay this action, which can trigger immediate tax liabilities, loss of grant eligibility, and halt essential community services. FTB has indicated that 22% of California charities' tax-exempt status was granted through the Form 3500A process.

While CalNonprofits has and continues to urge these nonprofits to initiate the Form 3500 process with FTB to shore up their state tax-exempt status, this process can take up to eleven months. AB 2084 provides a pragmatic solution by amending Revenue and Taxation Code Section 23701b to allow the FTB to review and exercise discretion in these cases. It also gives nonprofits the time to seek independent state review.

- 3) This bill is supported by Planned Parenthood Affiliates of California, which notes, in part:

At the federal level, tax-exempt status for nonprofit organizations has been a focus of recent attention, including statements about targeting organizations' 501(c)3 tax-exempt status due to disagreements over policies, political activity, or Diversity, Equity, and Inclusion (DEI) initiatives. For many nonprofit organizations, losing this designation would cause significant consequences and create challenges for organizations to continue their work. AB 2084 helps to prevent disruptions to California nonprofit organizations by giving the state Franchise Tax Board greater discretion to review and preserve state tax-exempt status for nonprofits that may be subject to a revocation of their federal tax-exempt status for political reasons associated with mission-driven activities.

- 4) Committee Staff Comments:

- a) *What problem does this bill seek to solve?* The author and sponsor of this bill argue that this bill is necessary to protect California tax-exempt nonprofit organizations that may have their federal tax-exempt status suspended or revoked for politically motivated or other reasons that lack basis in existing federal law and regulation. In particular, this bill is focused on the subset of nonprofit organizations that qualified for tax-exempt status for state tax purposes based on their federal determination by the IRS.

Under existing law, if the IRS suspends or revokes the tax-exempt status of a nonprofit organization and the organization received California tax-exempt status based on that federal determination, its state-level, tax-exempt status will also be revoked or suspended automatically by the FTB. While this bill does not change this requirement, it would allow the FTB to, in its discretion, maintain the organization's tax-exempt status only if the suspension or revocation is not related to any of the following:

- i) Fraud or intentional misrepresentation;

- ii) Misuse or diversion of organizational funds;
 - iii) Failure to file required returns or reports; or,
 - iv) Other significant breaches of organizational reporting or governance requirements.
- b) *Tax-exempt nonprofits*: Nonprofit organizations are generally organized and operated as both nonprofit and tax-exempt entities. "Nonprofit" status refers to incorporation status under state corporation law; "tax-exempt" status refers to federal income tax exemption under the IRC and, if applicable, state tax law. The vast majority of tax-exempt entities qualify under IRC Section 501(c)(3) and, accordingly, must be organized and operated exclusively for religious, charitable, scientific, literary, educational, testing for public safety, preventing cruelty to children or animals, or fostering national or international amateur sports competition (but only if none of its activities involve providing athletic facilities or equipment).¹

In addition to serving one of these public purposes, no part of the organization's net earnings can inure to the benefit of private shareholders or individuals, such as the creator's family members, board members, or persons controlled directly or indirectly by private interests. Further, organizations exempt under 501(c)(3) cannot, as a substantial part of their activities, attempt to influence legislation (subject to limited exceptions) or participate in political campaigns for or against any candidate for public office.

Organizations must apply to the IRS for tax-exempt status by completing the requisite form and provide copies of its organizing documents (e.g., articles of incorporation, constitution, trust document, etc.), bylaws (if adopted), and supplemental responses, if applicable, to demonstrate compliance with the above requirements.¹

- c) *Remaining in good standing*: Except for churches and other church-related organizations, tax-exempt organizations must still file annual information returns with the IRS. Organizations that normally have \$50,000 or more in gross receipts must complete Form 990 or Form 990-EZ; small organizations – those whose annual gross receipts are normally less than \$50,000 – must complete a shorter information return commonly referred to as the "e-Postcard".

If an organization fails to file an annual information return with the IRS for three consecutive years, its tax-exempt status is automatically revoked. The IRS notifies the organization by sending a letter to the mailing address on record and the organization is added to a publicly available list of all organizations that have had their tax-exempt status automatically revoked. If an organization's tax-exempt status is revoked, it is no longer exempt from federal income tax. Consequently, it may be required to file federal income tax returns and pay applicable income taxes. Additionally, an organization that loses its tax-exempt status is not eligible to receive tax-deductible contributions and will be removed from the IRS' list of tax-exempt organizations.¹

¹ *Publication 557 Tax-Exempt Status for Your Organization*, Internal Revenue Service (Rev. January 2025), <https://www.irs.gov/pub/irs-pdf/p557.pdf>.

- d) *Other ways tax-exempt status can be revoked:* If the IRS questions the federal tax-exempt status of a nonprofit organization, it can initiate an audit (or "examination") of the organization, auditing one or more information returns that were filed by the entity. For the tax years under examination, the IRS is effectively determining whether the information returns were accurate and reflected full compliance with the applicable tax laws. The two most common types of audits are correspondence examinations and field examinations, the latter of which is much more invasive, involving one or more auditors on site reviewing information and documents and conducting interviews. Field exams generally take several months to conduct, at a minimum, and often much longer.²

There are four potential outcomes of an IRS examination of an exempt organization: a no-change letter, a no-change letter with written advisories, a negotiated closing agreement, or a proposed revocation of exempt status. The first three outcomes enable the organization to retain its tax-exempt status, but in the second or third options, with certain conditions or required changes to ensure compliance with applicable laws and regulations.

If the IRS concludes an audit with a proposed revocation, the organization has 30 days (or longer if an extension is negotiated) to "protest" the proposed ruling and avail itself of the IRS appeals process. During the pendency of the IRS appeal, the organization remains tax-exempt; and during the pendency of the audit and appeal process, the IRS is barred by law from disclosing anything publicly about the matter. Once the protest is filed, it will be assigned to an IRS appeals officer, and the organization (and/or its representatives) will have the opportunity to have an appeals conference to make its case for denying the proposed revocation or otherwise proposing a settlement. The appeals conference is an informal meeting between the organization's representatives and the appeals officer; the IRS agent who conducted the underlying examination does not participate in the conference. The appeals officer (with the approval of their manager) has broad authority to order the IRS division conducting the examination to issue a no-change letter or no-change letter with written advisories, to negotiate a settlement with the organization, or to finalize the revocation.²

If the IRS appeals officer decides to uphold the proposed revocation, the organization will be issued a final adverse determination letter, at which point the entity will have lost its federal tax exemption and the organization has 90 days to petition the U.S. Tax Court, the U.S. Court of Federal Claims, or the U.S. District Court for the District of Columbia for a declaratory judgment as to its qualification for tax-exempt status.

Even if, following the IRS audit and appeal process (and any ensuing litigation), an organization's tax-exempt status is revoked, it still remains a nonprofit corporation (albeit a taxable one). Even post-revocation, the IRS and FTB have no authority to shut down a nonprofit, seize its assets, or otherwise take control of the organization.

² Jeffrey Scott Tenenbaum, *How the IRS Can—and Cannot—Revoke Federal Tax-Exempt Status*, American Bar Association (May 6, 2025), https://www.americanbar.org/groups/business_law/resources/business-law-today/2025-may/how-irs-revoke-federal-tax-exempt-status/.

- e) *Under threat*: Following a series of executive orders (EOs) by President Donald Trump in early 2025, nonprofit organizations engaging in diversity, equity, inclusion and environmental justice (EJ) work may now face significant legal and financial risks. Two major EOs—"Ending Illegal Discrimination and Restoring Merit-Based Opportunity" and "Ending Radical Wasteful Government DEI Programs and Preferencing"—aim to eliminate federal support for DEI and EJ programs. These directives not only target public-sector efforts, but also extend to private nonprofits, foundations, and associations, requiring them to certify compliance with federal anti-discrimination laws and potentially subjecting them to federal scrutiny.

Additionally, another EO issued on March 7, 2025 ordered the U.S. Secretary of Education to propose regulations that exclude from the Public Service Loan Forgiveness (PSLF) program nonprofit organizations that the administration believes do not qualify for 501(c)(3) tax-exempt status due to having a "substantial illegal purpose." The EO defined activities with a "substantial illegal purpose" to include those that aid or abet violations of federal immigration laws, support terrorism, aid or abet illegal discrimination, or violate state tort laws (including those against trespassing, disorderly conduct, or public nuisance), among others.

On July 10, 2020, President Trump posted on Twitter: "Too many Universities and School Systems are about Radical Left Indoctrination, not Education. Therefore, I am telling the Treasury Department to re-examine their Tax-Exempt Status...." Since re-taking office in January of 2025, President Trump has repeated similar remarks and explicitly called for the revocation of Harvard University's tax-exempt status on multiple occasions, culminating in officials at the Treasury Department sending the request targeting Harvard to the IRS's top lawyer at the time, Andrew De Mello.³

Last year, President Trump suggested that Citizens for Responsibility and Ethics in Washington (CREW), a nonprofit watchdog group that has litigated against his executive actions and conducted investigations into what it alleges are conflicts of interest, should have its tax-exempt status scrutinized because, "The only charity they had is going after Donald Trump." In April 2025, Ed Martin, the former interim U.S. Attorney in Washington D.C., sent a letter to Wikimedia Foundation in April, alleging that it was "engaging in a series of activities that could violate its obligations" as a tax-exempt nonprofit.⁴ After the killing of Charlie Kirk, President Trump and other top officials threatened to use tools such as stripping groups of tax-exempt status and opening criminal racketeering probes to target these groups.⁵

³ Brian Schwartz and Douglas Belkin, *Trump Administration Asks IRS to Start Process to Revoke Harvard's Tax-Exempt Status*, The Wall Street Journal (April 16, 2025), <https://www.wsj.com/us-news/education/trump-administration-asks-irs-to-start-process-to-revoke-harvards-tax-exempt-status-2a1c93cf>.

⁴ Oremus and Mark, *U.S. attorney for D.C. accuses Wikipedia of 'propaganda,' threatens nonprofit status*, Washington Post (April 25, 2025), <https://www.washingtonpost.com/technology/2025/04/25/wikipedia-nonprofit-ed-martin-letter/>.

⁵ Foxman, Reilly, and Korte, *Trump Readies Tax Audits, Criminal Probes of Liberal Groups*, Bloomberg Tax (September 18, 2025), <https://news.bloombergtax.com/daily-tax-report/trump-readies-tax-audits-criminal-probes-of-liberal-groups>.

- f) *Diversity, equity, and inclusion*: In June 2023, the U.S. Supreme Court ruled that Harvard University and the University of North Carolina's "race-conscious" admissions programs violate the equal protection clause of the 14th Amendment. *Students for Fair Admissions v. Harvard*, 600 U.S. 181 (2023). While Chief Justice Roberts, writing for the majority, noted that schools could be mindful of applicants' race in a much more narrowly tailored way, such as through an application essay or narrative, some critics have felt the decision did not go far enough and that a school considering race in any form amounted to unconstitutional discrimination.

In March 2025, the U.S. Department of Justice announced that it had launched investigations into Stanford University and three University of California schools to ensure the schools "comply with a Supreme Court decision that prevents colleges and universities from discriminating when choosing students for admission." In April 2025, the American Alliance for Equal Rights filed complaints with the IRS asking that they audit and revoke the tax-exempt status of the Gates Foundation and two other 501(c)(3) foundations due to their race-restricted scholarship programs.

- g) *Bob Jones University*: Over 30 years ago, the U.S. Supreme Court upheld the *administrative* revocation of an entity's tax-exempt status based on the organization's racially discriminatory admissions practices. *Bob Jones University v. United States*, 461 U.S. 574 (1983).

On January 19, 1976, the IRS officially revoked the tax-exempt status of Bob Jones University (BJU), a nonprofit religious and educational organization, based on its racially discriminatory policies.⁶ *Id.* at 581. BJU's sponsors genuinely believed that the Bible forbade interracial dating and marriage. *Id.* at 580. In furtherance of these beliefs, BJU excluded all African-Americans from admission until 1971. *Id.* Beginning that year, BJU began accepting applications from African-Americans, but only from those individuals "married within their race." *Id.* Then, in 1975, the U.S. Court of Appeals for the Fourth Circuit's decision in *McCrary v. Runyon*, 515 F.2d 1082 (1975), prohibited racial exclusion in private schools. *Id.* Following this decision, BJU began allowing unmarried African-Americans to enroll, but prohibited both interracial dating and marriage. *Id.*

Following the revocation of its tax-exempt status, BJU brought suit to recover \$21 in tax paid to the IRS. *Id.* at 582. The U.S. District Court for the District of South Carolina held that the revocation of BJU's tax-exempt status exceeded the delegated powers of the IRS and violated BJU's rights under the Religion Clauses of the *First Amendment*. *Id.*

⁶ Prior to 1970, the IRS granted tax-exempt status to private schools under Internal Revenue Code Section 501(c)(3), without regard to their racial admissions policies. *Bob Jones University, supra* at 577. Then, on January 12, 1970, a three-judge District Court for the District of Columbia issued a preliminary injunction barring the IRS from affording tax-exempt status to private schools in Mississippi with racially discriminatory admissions practices. *Id.* at 578. Roughly six months later, the IRS announced that it could "no longer legally justify allowing tax-exempt status to private schools which [*sic*] practice racial discrimination." *Id.* The IRS also announced that it could not "treat gifts to such schools as charitable deductions for income tax purposes." *Id.* This revised policy on discrimination was formalized in *Revenue Ruling 71-447*, which noted that "[a]ll charitable trusts, educational or otherwise, are subject to the requirement that the purpose of the trust may not be illegal or contrary to public policy." *Id.* at 579.

The Court of Appeals for the Fourth Circuit, in turn, reversed. *Id.*

On review, the Supreme Court upheld the IRS's revocation of BJU's tax-exempt status. The Court noted that racial discrimination in education violates deeply and widely accepted views of basic justice. *Id.* at 592. The Court acknowledged that, when the nation's first charitable exemption law was enacted in 1894, racially segregated school facilities would not have been viewed as against public policy. Nevertheless, the Court noted that contemporary standards must be considered when determining whether certain activities confer a public benefit entitled to preferential tax treatment. Thus, the Court concluded that an educational institution that, for whatever reason, practices racial discrimination, cannot be viewed as exercising beneficial influences in community life, and should not be encouraged by having all taxpayers share in its support by way of preferential tax treatment. *Id.* at 595. Moreover, the Court validated the IRS's administrative action by noting:

[I]t would be anomalous for the Executive, Legislative, and Judicial Branches to reach conclusions that add up to a firm public policy on racial discrimination, and at the same time have the IRS blissfully ignore what all three branches of the Federal Government had declared.

Id. at 598.

One commenter has argued that this precedent could provide some justification for the revocation of tax-exempt status from colleges and universities in light of *Students for Fair Admissions*.⁷ However, others have rejected this interpretation because the IRS does not have the authority to determine fundamental public policy and then revoke exemptions on the basis of that determination.⁸ Writing in response to the argument above, a group of law professors with expertise in tax and nonprofit law, argue:

Bob Jones University teaches that we must distinguish "public policy" from "fundamental public policy." Public policy includes all actions and decisions by governmental bodies to address societal issues. As in *Bob Jones University*, fundamental public policy involves core values. A new presidential administration is free to establish a new public policy. But such a new public policy does not create a fundamental public policy. Fundamental public policies do not change with changes in presidential administrations. Charities do not gain, and then lose, and then perhaps regain exemption depending on the positions of whatever U.S. president is in office. If the IRS fails to observe the distinction between public policy and fundamental public policy in revoking Harvard's exemption, Harvard will have several avenues for seeking judicial review.

⁷ Marie Sapirie, *Harvard Has a Precedent Problem in Fight to Keep Exempt Status*, TaxNotes Federal (May 13, 2025), <https://www.taxnotes.com/tax-notes-today-federal/exempt-organizations/harvard-has-precedent-problem-fight-keep-exempt-status/2025/05/13/7s5wx>.

⁸ April, Galle, Hackney, and Hitoshi Mayer, *Harvard Does Have Options if It Loses Tax-Exempt Status*, TaxNotes Federal (May 21, 2025), <https://www.taxnotes.com/tax-notes-today-federal/exempt-organizations/harvard-does-have-options-if-it-loses-tax-exempt-status/2025/05/21/7s7fz>.

- h) *What happens during FTB's review period?* As currently drafted, this bill may permit an organization to continue operating and remain in good standing in California during the FTB's review period until a final determination is made. However, the bill does not address key operational and compliance implications that may arise if the organization is ultimately denied state exemption status retroactive to the federal revocation date. Specifically, it is unclear how the organization should treat contributions received during the review period, or what legal or administrative status the organization would hold while its exemption is under review. To provide clarity, the author may wish to amend the bill to specify the treatment of contributions received during that time and other potential administrative concerns.
- i) *Prior legislation:*
- i) AB 1318 (Bonta), Chapter 451, Statutes of 2025, provided that, where 501(c)(3) tax-exempt status is used to determine eligibility for any state grant or service contract, or for the disbursement of state or local funds, an organization that is exempt from California taxes is also deemed eligible.
 - ii) SB 834 (Wiener), of the 2021-22 Legislative Session, would have, under the CT Law, required the Attorney General to notify the FTB of any finding that a tax-exempt organization was actively engaged in, or incited the active engagement in, illegal activities, including those related to the January 6, 2021, attempted insurrection at the United States Capitol. The bill also restated the FTB's existing authority to revoke the tax-exempt status of an organization found to be in violation. SB 834 was vetoed by Governor Newsom, whose veto message stated, in part:

This bill allows the FTB to revoke the tax-exempt status of a nonprofit, charitable organization if the California Attorney General determines the organization has engaged in treason, insurrection, conspiracy, government overthrow, or mutiny by members of the military. Without question, extremist groups that participate in anti-government acts such as those that took place during the insurrection on January 6, 2021, should be renounced and investigated for their participation. However, these are issues that should be evaluated through the judicial system with due process and a right to a hearing.

REGISTERED SUPPORT / OPPOSITION:

Support

California Association of Nonprofits
 CPCA Advocates, Subsidiary of the California Primary Care Association
 Planned Parenthood Affiliates of California

Opposition

None on file

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