Office of Senate Floor Analyses
(916) 651-4171

UNFINISHED BUSINESS

Bill No: SB 1349
Author: Gonzalez (D), et al.
Amended: 6/17/26
Vote: 21

SENATE REVENUE AND TAXATION COMMITTEE: 4-1, 4/8/26
AYES: McNerney, Ashby, Becker, Grayson
NOES: Alvarado-Gil

SENATE APPROPRIATIONS COMMITTEE: 5-2, 5/14/26
AYES: Cervantes, Cabaldon, Grayson, Richardson, Wahab
NOES: Seyarto, Dahle

SENATE FLOOR: 30-8, 5/19/26
AYES: Allen, Archuleta, Arreguín, Ashby, Becker, Blakespear, Cabaldon, Caballero, Cervantes, Cortese, Durazo, Gonzalez, Grayson, Hurtado, Laird, Limón, McGuire, McNerney, Menjivar, Padilla, Pérez, Reyes, Richardson, Rubio, Smallwood-Cuevas, Stern, Umberg, Wahab, Weber Pierson, Wiener
NOES: Alvarado-Gil, Choi, Dahle, Jones, Ochoa Bogh, Seyarto, Strickland, Valladares
NO VOTE RECORDED: Grove, Niello

ASSEMBLY FLOOR: 57-18, 8/20/26 - See last page for vote

SUBJECT: Taxation: tax expenditures: Legislative Analyst's Office: assessment, report, and recommendation

SOURCE: American Federation of State, County and Municipal Employees, AFL-CIO
California Teachers Association

DIGEST: This bill directs the Legislative Analyst's Office (LAO) to comprehensively assess the state's major tax expenditures, as defined, issue a report, and make a recommendation to the Legislature.

Assembly Amendments (1) Require LAO to complete its assessments by January 1, 2032; (2) Refine deadlines for legislative committees to hold hearings regarding the assessments; (3) Require LAO to submit assessments in compliance with specified provisions of the Government Code; (4) Provide LAO discretion to determine the sequence in which to publish its assessments; (5) Direct the Franchise Tax Board (FTB), California Department of Tax and Fee Administration (CDTFA), and Employment Development Department (EDD) to ensure that relevant anonymized taxpayer data is made available to LAO with appropriate levels of data security and privacy protections are in place; (6) Add cross references; and (7) Insert a January 1, 2033, sunset date.

ANALYSIS:

Existing law:

1) Allows various income tax credits, deductions, exemptions, and exclusions, among them:

    a) The Research and Development Credit, calculated in partial conformity with federal law, that allows a credit against the Personal Income and Corporation Taxes for a taxpayer's qualified research expenses incurred in California that exceed the base year amount, as defined, plus a percentage of the amount paid or incurred during the taxable year on research undertaken by a research consortium.

    b) Basis Step-Up on Inherited Property, in conformity with federal law, that "steps up" the basis of inherited property to fair market value as of the date of death under both the Personal Income and Corporation Taxes, so heirs do not pay taxes on gains from assets that appreciated in value when held by the decedent.

    c) Like-Kind Exchanges, in modified conformity with federal law, that defers the recognition of any gain or loss under both the Personal Income and Corporation Taxes on the exchange of property held for productive use in a trade or business or for investment, if that property is exchanged solely for property of a like kind that is to be held either for productive use in a trade or business or for investment.

    d) Expensing of Research Expenses, in conformity with federal law, where taxpayers can elect to either deduct research and experimental expenditures under both the Personal Income and Corporation Taxes in full the year they were paid or incurred, or elect to capitalize and amortize them over at least 60 months.

2) Allows an exception for qualified cable companies to the general requirement for multistate businesses to apportion net income to California for Corporation Tax purposes based on a factor equal to its California sales divided by its total sales. Qualified cable companies spending $250 million or more in California on certain expenditures can exclude half of their in-state sales when apportioning (Proposition 39, 2012).

3) Permits taxpayers to either file on a worldwide combined reporting basis or to elect to calculate California income and activities on a water's-edge basis. Generally, water's-edge taxpayers may exclude income and apportionment factors of foreign-organized unitary affiliates that would otherwise be part of its unitary combined report, with some exceptions.

4) Requires the Department of Finance (DOF) to annually publish a list of tax expenditures exceeding $5 million each November 1 with specified contents.

This bill:

1) Directs the Legislative Analyst's Office to comprehensively assess the major tax expenditures of the state, write and publish a report on each major tax expenditure, and make a recommendation to the Legislature based on each report.

2) Defines "major tax expenditure" to include:

   a) The Water's Edge Election.

   b) The Research and Development Tax Credit.

   c) Basis Step-up on Inherited Property.

   d) Like-Kind exchanges.

   e) Expensing of Research Expenditures.

   f) Special apportionment for qualified cable companies.

3) Requires LAO to identify any savings that the Legislature can realize by reducing or limiting the major tax expenditures as part of its assessments.

4) Directs LAO to consider the following criteria when finalizing each report:

a) The extent to which the major tax expenditure is a cost-effective use of resources compared to other options to address the same purpose, intent, or goal.

b) An analysis of the major tax expenditure's effect on the General Fund, including Proposition 98.

c) An analysis of the major tax expenditure's effect on employment, wages, and the state's economy.

d) Whether opportunities exist to improve the effectiveness of the major tax expenditure in meeting its purpose, intent, or goal, or if no such opportunities exist, whether the Legislature should enact legislation to repeal each major tax expenditure.

5) Requires LAO to complete and publish on its internet website its first report on a major tax expenditure by January 1, 2028, and complete and publish on its internet website each subsequent report on a major tax expenditure in a sequence it determines until the fifth and final report is submitted January 1, 2032.

6) Directs the LAO to submit its report in compliance with a specific provision of the Government Code.

7) Requires the Senate and Assembly Committees on Revenue and Taxation to hold a joint public hearing on each assessment, commencing August 15, 2028, and again by each August 15th of the second year of each legislative session on the two most recent reports LAO submits.

8) Directs FTB, CDTFA, and EDD to ensure that relevant anonymized taxpayer data is made available to LAO, with appropriate levels of data security and privacy protections for transferred or sensitive data.

9) Makes legislative findings and declarations supporting its purposes.

10) Sunsets its provisions on January 1, 2033.

Background

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. According to DOF's report, California foregoes around $94.2 billion per year as a result of its tax expenditures.

Many of the state's tax expenditures that result in the most foregone revenue do not have sunset dates, some of which fully or partially conform with provisions of the Internal Revenue Code. However, many of California's most significant tax expenditures *do* contain sunset dates. While the Legislature has extended sunsets for several tax expenditures like those noted above, they occasionally sunset and are repealed. In 2025, the New Employment Credit, which directed the Franchise Tax Board (FTB) to allocate credits for wages paid by taxpayers to qualified employees within areas that suffer from high levels of poverty and unemployment, sunset.

Additionally, the Legislature often requires the Legislative Analyst's Office (LAO) to analyze specific aspects of new or extended tax expenditure programs and report to the Legislature, usually one year before its sunset date. The Legislature applied these requirements to the Motion Picture Production Credit and the California Competes Tax Credit, among others. Additionally, FTB publishes several reports regarding specific tax credits.

Section 41. In 2014, Governor Brown signed SB 1335 (Leno, Chapter 845, Statutes of 2014), which added Section 41 to the Revenue and Taxation Code. In the hopes of applying the same level of review used for government spending programs to tax expenditure programs, including tax credits, Section 41 requires any bill introduced on or after January 1, 2015, that allows a new income tax credit to contain specific goals, purposes, and objectives that the tax credit will achieve. In addition, Section 41 requires detailed performance indicators for the Legislature to use when measuring whether the tax credit meets its goals, purposes, and objectives. The Legislature expanded Section 41 to include all tax expenditures under the Personal Income and Corporation Taxes, as well as sales and use tax exemptions (AB 263, Burke, Chapter 743, Statutes of 2019), but not Personal Income Tax exclusions when there is no available data to collect (AB 3289, Committee on Revenue and Taxation, Chapter 124, Statutes of 2024).

FISCAL EFFECT: Appropriation: No Fiscal Com.: No Local: No

According to the Assembly Appropriations Committee:

- Likely absorbable cost pressures to the LAO to complete the five required reports on an annual basis. However, this committee sees a wide array of bills that require the LAO to measure different tax expenditures. Generally, a request to prepare an individual report would not generate significant new workload for the LAO. But, taken together, these proposals strain the ability of the LAO fulfill other existing or future legislative mandates and requests, as the LAO's budget is subject to the Legislature's constitutional spending cap (General Fund). The LAO notes that this bill would likely fully saturate the office's existing capacity to perform tax expenditure analyses for the foreseeable future, meaning any subsequent legislation tasking the LAO with such new workload would necessitate additional staffing resources.

- Since the primary purpose of this bill is to create a report, this bill qualifies for this committee's suspense file consistent with committee rules and custom and practice.

- Minor and absorbable costs to FTB and CDTFA to share anonymized taxpayer data with the LAO if needed. The EDD notes its estimated costs to enter into a data sharing agreement with the LAO would depend on the specific data elements requested and be subject to reimbursement by the LAO.

SUPPORT: (Verified 8/18/26)

American Federation of State, County and Municipal Employees, AFL-CIO (Co-Source)
California Teachers Association (Co-Source)
California Association of School Business Officials
California Federation of Labor Unions, AFL-CIO
California Federation of Teachers
California Professional Firefighters
California School Boards Association
California School Employees Association
California State Association of Counties
California State Council of Service Employees International Union
California Tax Reform Association
City of Thousand Oaks
Labor Coalition
League of California Cities
Los Angeles Unified School District
The Arc and United Cerebral Palsy California Collaboration
United Domestic Workers/AFSCME Local 393
1 Individual

OPPOSITION: (Verified 8/18/26)

California Chamber of Commerce
California Life Sciences
California Taxpayers Association

ARGUMENTS IN SUPPORT: According to the author, "California has over 100 tax expenditures that resulted in a $94 billion loss in general fund revenues in fiscal year 2025-26. Because programs established before 2014 lack modern performance standards, a 2016 State Auditor's report found insufficient evidence that they are actually meeting their goals. This assessment of California's largest corporate tax expenditures introduces long-overdue oversight into the use of taxpayer dollars. By providing a clear, data-driven report, SB 1349 will chart a path for California to invest its resources more effectively and accountably."

ARGUMENTS IN OPPOSITION: According to the California Taxpayers Association and California Chamber of Commerce, "We are concerned that SB 1349 would create an unnecessary step in state government to report findings relating to critical business tax policies California has adopted to encourage businesses to locate and expand in California, duplicating existing evaluations conducted by the Department of Finance and others. At a time when California's state budget is facing cost pressures, and the Legislature and administration are seeking to minimize new program costs, any duplicative program that creates new costs for an evaluation that already exists is not necessary. While it is meritorious for the state to assess the effectiveness of tax policies and program expenditures, this measure would create significant uncertainty with respect to the future of the state's tax structure and would adversely affect California's ability to retain and attract jobs and investments. The threat of repealing tax incentives, given our state's already high cost of doing business, poses a significant barrier to jobs, investment, and the state's long-term economic growth."

ASSEMBLY FLOOR: 57-18 8/20/26
AYES: Addis, Aguiar-Curry, Ahrens, Alvarez, Arambula, Ávila Farías, Bains, Bauer-Kahan, Bennett, Berman, Boerner, Bonta, Bryan, Calderon, Caloza, Carrillo, Connolly, Elhawary, Fong, Gabriel, Garcia, Gipson, Mark González, Haney, Harabedian, Hart, Irwin, Jackson, Kalra, Lee, Lowenthal, McKinnor, Muratsuchi, Nguyen, Ortega, Pacheco, Papan, Patel, Pellerin, Petrie-Norris, Quirk-Silva, Ransom, Celeste Rodriguez, Michelle Rodriguez, Rogers, Schiavo,

Schultz, Sharp-Collins, Solache, Soria, Stefani, Valencia, Ward, Wicks, Wilson, Zbur, Rivas
NOES: Alanis, Castillo, Davies, DeMaio, Dixon, Ellis, Flora, Jeff Gonzalez, Hadwick, Hoover, Johnson, Lackey, Macedo, Patterson, Sanchez, Ta, Tangipa, Wallis
NO VOTE RECORDED: Chen, Krell, Ramos, Blanca Rubio

Prepared by: Colin Grinnell / REV. & TAX. / (916) 651-4117
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****** END ******