SENATE THIRD READING
SB 1435 (Committee on Revenue and Taxation)
As Amended June 22, 2026
Majority vote. Tax Levy

SUMMARY

Updates California tax law that conforms, with certain modifications, to federal tax law.

Major Provisions

1) Clarifies, under the California Earned Income Tax Credit (CalEITC), that the maximum amount of disqualified income a taxpayer may earn is $3,400, regardless of the federally stipulated threshold.

2) Decouples, under the Personal Income Tax (PIT) Law, from the federal limitation on the business interest expense deduction.

3) Conforms to the federal clarification that the excess business loss of a noncorporate taxpayer is determined without regard to any tax attributes resulting from any trade or business for services performed as an employee.

4) Decouples from special federal withholding rules related to dispositions of partnership interests.

5) Removes deadwood provisions, adjusts or removes certain operative dates, removes certain repeal dates, updates or removes certain cross references, and renumbers certain sections.

6) Applies the provisions of this bill to taxable years beginning on or after January 1, 2025, except as otherwise provided.

7) Provides that specified technical corrections included in this bill are declaratory of existing law and must be applied in the same manner and for the same periods as specified for federal purposes, as conditioned, to the extent that the provisions of this bill are correct.

8) Takes immediate effect as a tax levy.

COMMENTS

1) *Conformity in California*: California tax law does not automatically conform to changes in federal tax law. Rather, state tax law conforms to federal tax law in two ways. The first is by way of the general date-change conformity. The second is by specific cross-reference to certain sections of the Internal Revenue Code (IRC). Thus, for the state to adopt changes to federal tax law, individual tax bills conforming to specific federal changes, or an omnibus bill conforming to federal tax law as of a certain date are required.

   Prior to 1983, the state's tax laws were stand-alone, meaning the provisions generally did not adopt federal law by way of cross-reference to IRC sections. Rather, the Legislature stipulated the provisions of the Revenue and Taxation Code (R&TC) in their entirety. In 1983, however, California repealed significant sections of tax law and replaced them with references to federal tax law. Throughout the remainder of that decade and into the 1990s, California enacted conformity legislation nearly every year. By the late 1990's and early 2000's, general date-change conformity legislation became less frequent, occurring on a five-year basis.

2) *Why conform*? Generally, conformity between federal and state law eases taxpayer compliance and reduces confusion. State taxation begins with a taxpayer's federal adjusted gross income, and makes adjustments to this amount to derive taxable income in California. As the difference in federal and state law increases, further adjustments are needed, which can lead to errors and cause confusion as tax filers prepare their returns. Conformity eases the burden for state tax administration as well, given state tax agencies can more often rely on federal audits, case law, and regulations.

   These advantages come with potential cost, namely to state revenues. Indeed, much of tax law is providing for various tax expenditures, which are generally defined as tax credits, deductions, exclusions, or exemptions. Both state and federal governments often use tax expenditures to encourage certain beneficial taxpayer behavior. A federal incentive, however, may not promote the same activity if adopted at the state level, and the foregone revenues resulting from conforming to that provision may not be worthwhile.

   California, unlike the federal government, must pass a balanced budget. Section 12(g), Article IV of the California Constitution prohibits both the legislative and executive branches of state government from passing a budget that includes appropriations from the General Fund in excess of General Fund revenues. Moreover, California cannot control the supply of money in the state as the federal government can throughout the nation. In other words, California cannot "print" money, or increase the monetary base, to subsidize any budget deficit for a given year.

   Thus, the Legislature has chosen to selectively conform to federal tax law as of a certain date, allowing prudent examination of the changes made by the federal government before adoption by California.

3) *Interest in intent*: Last year, the Legislature passed SB 711 (McNerney), Chapter 231, Statutes of 2025. With the enactment of that bill, California tax law now conforms to federal tax law, with certain modifications, as it read on January 1, 2025. After passage by both houses, an inadvertent drafting error was identified. Specifically, SB 711 decoupled California's conformity under the Corporation Tax Law from the federal limitation on business interest expense deductions, but did not provide for similar nonconformity under the PIT Law. To clarify the intent of SB 711, the author submitted a letter to the Senate Journal on September 12, 2025, stating that conforming to the business interest expense deduction limitation under the PIT Law was not the author's intent. This bill would rectify the inadvertent conformity to the limitation.

4) *This bill*: In addition to rectifying the drafting omission in SB 711, this bill makes further technical and clean-up changes identified by stakeholders and the FTB since the passage of SB 711. These additional changes include clarifying the amount of disqualified income a taxpayer may earn before being ineligible for the CalEITC, clarifying the calculation of excess business losses for noncorporate taxpayers, decoupling from special withholding rules on dispositions of certain partnerships, and code maintenance.

According to the Author
SB 1435 incorporates several technical and conforming clean-up items resulting from the enactment of SB 711 (McNerney), Chapter 231, Statutes of 2025, which updated the state's date of conformity to the [IRC]. SB 711 amended more than 119 sections of the [R&TC] and, given the states complex structure of modified conformity to federal law, some follow-up changes are necessary. Committee staff distributed these proposals to affected parties for review before they were included in the bill. Should anyone object to an item in the bill, the Committee will remove said item.

Arguments in Support
The California Taxpayers Association, writing in support of this bill, states, in part:

> California takes a selective approach to conforming to federal tax changes one provision at a time, allowing lawmakers to evaluate each amendment for its fiscal impact, equity implications, and alignment with the state's economic priorities before deciding whether to adopt it. For the nation's most populous and economically diverse state, this tailored approach preserves the flexibility to support key industries, protect low-income taxpayers, and maintain a stable revenue base rather than importing federal rules that may not suit California's unique housing, labor, and environmental policies and the state's economic growth needs.

Arguments in Opposition
None on file

FISCAL COMMENTS

The Assembly Appropriations Committee, in its analysis of this bill, states:

1) General Fund revenue loss of approximately $240 million in fiscal year (FY) 2025-26, $550 million in FY 2026-27, $360 million in FY 2027-28, and $370 million in FY 2028-29, related to decoupling from the federal limitation on the business interest expense deduction under PIT Law.

   However, this bill is a clean-up measure to last year's conformity measure, SB 711 (McNerney), Chapter 231, Statutes of 2025, which was estimated to result in hundreds of millions of dollars of GF revenue gain. As noted in the Assembly Revenue and Taxation Committee's analysis of this bill, the revenue loss attributable to this bill was already accounted for as revenue loss in SB 711, but the actual provision was inadvertently omitted from the enacted measure. The Franchise Tax Board (FTB) notes that this bill's other provisions would not impact PIT or Corporation Tax Law revenues.

2) Absorbable costs to the FTB to update guidance and other materials and process amended tax returns filed by taxpayers impacted by the limitation on business interest revision.

VOTES

SENATE FLOOR: 33-0-7
YES: Archuleta, Arreguín, Ashby, Blakespear, Cabaldon, Caballero, Cervantes, Choi, Cortese, Dahle, Durazo, Gonzalez, Grayson, Grove, Jones, Laird, Limón, McGuire, McNerney, Menjivar, Ochoa Bogh, Pérez, Reyes, Richardson, Rubio, Seyarto, Smallwood-Cuevas, Strickland, Umberg, Valladares, Wahab, Weber Pierson, Wiener
ABS, ABST OR NV: Allen, Alvarado-Gil, Becker, Hurtado, Niello, Padilla, Stern

ASM REVENUE AND TAXATION: 7-0-0
YES: Gipson, Sanchez, Carrillo, DeMaio, McKinnor, Quirk-Silva, Michelle Rodriguez

ASM APPROPRIATIONS: 15-0-0
YES: Wicks, Hoover, Arambula, Calderon, Caloza, Dixon, Fong, Mark González, Krell, Pacheco, Pellerin, Sharp-Collins, Solache, Ta, Tangipa

UPDATED

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