UNFINISHED BUSINESS

Bill No: SB 1435
Author: Committee on Revenue and Taxation
Amended: 6/22/26
Vote: 21- Urgency

SENATE REVENUE AND TAXATION COMMITTEE: 5-0, 4/22/26
AYES: McNerney, Alvarado-Gil, Ashby, Becker, Grayson

SENATE APPROPRIATIONS COMMITTEE: 7-0, 5/14/26
AYES: Cervantes, Seyarto, Cabaldon, Dahle, Grayson, Richardson, Wahab

SENATE FLOOR: 33-0, 5/22/26
AYES: 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
NO VOTE RECORDED: Allen, Alvarado-Gil, Becker, Hurtado, Niello, Padilla, Stern

ASSEMBLY FLOOR: 77-0, 8/24/26 - See last page for vote

SUBJECT: Personal Income Tax Law and Corporation Tax Law: federal conformity

SOURCE: Author

DIGEST: This bill makes technical and conforming changes to several provisions of the Revenue & Taxation Code pertaining to date-change conformity to federal tax law as of specified date, January 1, 2025.

Assembly Amendments (1) Decouple state conformity to Section 1446(f) of the Internal Revenue Code (IRC); and (2) Make other technical changes.

ANALYSIS:

Existing law:

1) Does not automatically conform to changes made by Congress to the IRC except for changes to pension and retirement programs; instead, the Legislature must affirmatively conform state law to federal to ensure consistent treatment for the same items.

2) Conforms to the IRC as of January 1, 2025, with modifications (SB 711, McNerney, Chapter 231, Statutes of 2025).

3) Conforms under the Personal Income Tax (PIT) law to Section 13301(a) of the Tax Cuts and Jobs Act (P.L. 115-97, "TCJA"), which limits the deductibility of interest paid by a trade or business, but explicitly decouples from this change in the Corporation Tax.

4) Does not conform under the Corporation Tax to Section 13301(a).

5) Conforms with modification to IRC 1446, relating to the withholding of tax by a partnership with foreign partners.

6) Contains references to various IRC "deadwood" provisions.

This bill:

1) Provides that for taxable years beginning on or after January 1, 2025, the limit on deductibility for business interest under federal income tax law does not apply for purposes of the PIT Law.

2) Removes references in state law to IRC "deadwood" provisions; and makes several technical amendments.

3) Decouples state conformity to IRC 1446(f), relating to special rules for tax withholdings on dispositions of partnership interests by persons in a partnership with foreign partners.

4) Apply to taxable years beginning on or after January 1, 2025, unless otherwise specified.

Background

SB 711 Clean-up. Between 2015 and 2025, there were more than 1,000 substantive changes to the Internal Revenue Code, for which California had not yet

determined whether the Revenue and Tax Code (RTC) would conform, not conform, or conform with modifications. When the Legislature enacted SB 711, it conformed to the changes for the first time in ten years by updating the "specified date" in RTC Section 17024.5. Advancing the specified date incorporates select changes made to the IRC where the RTC applies by reference. The bill then enacts statutes to either decouple or conform with modifications to specific changes made by Congress to the IRC, where state conformity is not desired. Through this "date-change" process, SB 711 updates the RTC to align with the IRC, thereby reducing differences between a taxpayer's state and federal tax obligations and easing compliance burdens for taxpayers. Examples include the treatment of alimony payments, catch-up IRA contributions, and first-responder retirement and disability payments.

However, SB 711 inadvertently conformed the state PIT law to Section 13301(a) of the TCJA, which limits the deductibility of interest paid by a trade or business. SB 711 explicitly decouples from this change under Section 89 of the Corporation Tax. SB 711's PIT omission was identified past the deadline to amend the measure. SB 711's estimated General Fund revenue gains were approximately $336.4 million in fiscal year 2025-26, $246.7 million in 2026-27, and $172.1 million in 2027-28 *assumed* the decoupling, which, as noted above, was inadvertently not included in SB 711. Additionally, the Franchise Tax Board identified several "deadwood" provisions, and helpful conforming changes have been identified since SB 711's enactment.

Additionally, prior to SB 711, California conformed to the withholding of tax by a partnership with foreign partners under IRC section 1446, as of the "specified date" of January 1, 2015, with modifications for the rates of tax, but did not conform to the federal requirement to withhold 10% of the amount realized on the sale or exchange of a partnership interest unless the transferor certifies that the transferor is not a nonresident alien individual or foreign corporation. SB 711 updated the state's conformity to IRC 1446(f) under RTC 18666 in three ways:

- Amends RTC 18666(a) to make a technical amendment clarifying that IRC 1446, relates to withholding of tax on foreign partners' share of effectively connected income.

- Amends RTC 18666(b)(1) by stating that IRC 17043, in addition to 17041, are applicable to the tax referred to in IRC 1446(b)(2)(A).

- Adds RTC 18666(b)(3) stating that the rate of tax referred to in IRC 1446(f)(1), relating to disposition of partnership interests, shall be the rate specified in

Sections 17041 and 17043, as applicable, rather than the rate specified in IRC 1 or IRC 11, relating to tax imposed.

Following the enactment of SB 711, tax practitioners raised concerns that conformity to IRC 1446(f) was ambiguous and difficult to comply with, including that the federal definition of effectively connected income did not align with the treatment of California-source income. This misalignment makes it difficult for taxpayers to comply with the provisions' withholding requirements. This bill repeals conformity to IRC 1446(f), which only affects the withholding requirement, not the amount of tax due.

History of "date-change" conformity. "Date change" commenced in 1982, when California's income and corporation taxes were not linked to the Internal Revenue Code. In that year, the Legislature made wholesale changes to the RTC, replacing more than 300 stand-alone provisions and linking them to the Internal Revenue Code. For example, instead of California law defining "income" to include wages, salaries, and capital gains, among others, it says, "Section 61 of the Internal Revenue Code, relating to gross income defined, applies except as otherwise provided." These changes significantly reduced the differences between state and federal tax systems, simplifying compliance for taxpayers, practitioners, and tax enforcement agencies. One part of the 1982 changes was to enact a section of law in the RTC that provides that, as of January 1st of a specified year, the IRC applies for California purposes. The Legislature could then enact a bill to update the specified year to incorporate any subsequent changes that Congress made to the IRC, while at the same time providing in the bill the specific changes that they did not want to apply for California purposes.

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

According to the Assembly Appropriations Committee:

- 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 FTB notes that this bill's other provisions would not impact PIT or Corporation Tax Law revenues.

- 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.

SUPPORT: (Verified 8/24/26)

California Society of Enrolled Agents
California Taxpayers Association

OPPOSITION: (Verified 8/24/26)

None received

ARGUMENTS IN SUPPORT: According to the California Taxpayers Association, "SB 1435… [updates] California tax laws to ensure federal conformity for personal income and corporation taxes. 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. SB 1435… [ensures] that California safeguards both its budget and its policy goals while giving taxpayers more consistency with federal rules."

ASSEMBLY FLOOR: 77-0, 8/24/26
AYES: Addis, Aguiar-Curry, Ahrens, Alanis, Alvarez, Arambula, Ávila Farías, Bains, Bauer-Kahan, Bennett, Berman, Boerner, Bonta, Bryan, Calderon, Caloza, Carrillo, Castillo, Connolly, Davies, DeMaio, Dixon, Elhawary, Ellis, Flora, Fong, Gabriel, Garcia, Gipson, Jeff Gonzalez, Mark González, Hadwick, Haney, Harabedian, Hart, Hoover, Irwin, Jackson, Johnson, Kalra, Krell, Lackey, Lee, Lowenthal, Macedo, Muratsuchi, Nguyen, Ortega, Pacheco, Papan, Patel, Patterson, Pellerin, Petrie-Norris, Quirk-Silva, Ramos, Ransom, Celeste Rodriguez, Michelle Rodriguez, Rogers, Blanca Rubio, Sanchez, Schiavo,

Schultz, Sharp-Collins, Solache, Soria, Stefani, Ta, Tangipa, Valencia, Wallis, Ward, Wicks, Wilson, Zbur, Rivas
NO VOTE RECORDED: Chen, McKinnor

Prepared by: Haley Summers / REV. & TAX. / (916) 651-4117
11/16/26 10:45:33

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