

Date of Hearing: July 14, 2025

ASSEMBLY COMMITTEE ON REVENUE AND TAXATION

Mike Gipson, Chair

SB 711 (McNerney) – As Amended July 7, 2025

2/3 vote. Urgency. Fiscal committee.

**SENATE VOTE:** 38-0

**SUBJECT:** Taxation: federal conformity

**SUMMARY:** Conforms to federal tax law by adopting changes made to the Internal Revenue Code (IRC) through 2024. Specifically, **this bill:**

- 1) Updates California's date of conformity to the IRC from taxable years beginning on or after January 1, 2015, to taxable years beginning on or after January 1, 2025, with certain modifications.
- 2) Modifies conformity to the IRC such that:
  - a) The minimum credit rate under the low-income housing tax credit does not apply;
  - b) The special rules enhancing and making refundable the child and dependent care tax credit do not apply;
  - c) The percentages under the alternative simplified research and development tax credit are 3% and 1.5%, rather than 14% and 6%, respectively, and the election for the alternative simplified research and development tax credit may be made for taxable years beginning on or after January 1, 2025;
  - d) The election of a small business to apply a research and development credit to its payroll tax credit portion does not apply;
  - e) The historic building rehabilitation credit is 20% of the qualified rehabilitation expenditures, is 25% of qualified rehabilitation expenses for certain buildings, is not subject to the five-year ratable share, and a reallocation for unused credits that were set aside by the California Tax Credit Allocation Committee is permitted;
  - f) Changes made to the alternative minimum tax (AMT) since January 1, 2015 do not apply, except as provided;
  - g) The provisions related to adjusted financial statement income for the purposes of the AMT do not apply;
  - h) The application of the AMT credit to certain corporations does not apply;

- i) The penalty waiver for qualified disaster distributions as loans from certain retirement account applies;
- j) The conversion gain exclusion for S-corporations does not apply if the recognition of the gain occurs within ten years of the conversion;
- k) The modifications to the treatment of income in excess of daily accruals on residual interest related to the net operating loss deduction, and to the AMT, do not apply;
- l) The treatment of qualified small employer health reimbursement arrangement does not apply;
- m) Additional expenses under the Paycheck Protection Program are excluded from gross income;
- n) The gross income exclusion for East Palestine disaster relief payments does not apply;
- o) The treatment of qualified rollovers to Roth Individual Retirement Accounts from a long-term qualified tuition program do not apply, and disbursed amounts must be included in gross income;
- p) The gross income exclusion for the discharge of indebtedness on a qualified principal residence applies to discharges occurring before January 1, 2015;
- q) The suspension of the gross income exclusion for qualified bicycle commuting reimbursement does not apply;
- r) The suspension of the gross income exclusion for qualified moving expense reimbursements does not apply;
- s) The gross income exclusion for certain disability related first responder retirement pay applies to taxable years beginning on or after January 1, 2027;
- t) The gross income exclusion for certain coal power grants to non-corporate taxpayers does not apply;
- u) The gross income exclusion for compensation for losses or damages resulting from certain wildfires does not apply;
- v) The modifications to the amortization of research and experimental expenditures made after January 1, 2015 do not apply;
- w) The suspension of the moving expense deduction for certain taxable years does not apply;
- x) The limitation on deduction by employers of expenses for fringe benefits does not apply;
- y) The limitation on the depreciation of passenger automobiles, and the limitation on depreciation when property is used for certain personal purposes, do not apply;

- z) The deduction for qualified business income does not apply;
- aa) The limitation on casualty losses for certain taxable years does not apply;
- bb) The special rules for personal casualty losses sustained in certain disasters federally declared in 2016 do not apply;
- cc) The special rules for qualified disaster-related personal casualty losses, and their extension, do not apply;
- dd) The inclusion of other expenses incurred by an individual in connection with the gambling activity as eligible for deduction as a wagering loss does not apply;
- ee) The limitation on the deduction of state and local taxes for certain taxable years does not apply;
- ff) The limitations on the mortgage interest deduction do not apply;
- gg) The medical expense deduction must exceed 10% of adjusted gross income to be allowed, for taxable years beginning before January 1, 2021;
- hh) The federal depreciation treatment of certain property does not apply;
- ii) The enhancements to the charitable contribution deduction do not apply;
- jj) The special rule for the charitable contribution deduction for taxpayers who do not itemize does not apply;
- kk) The enhancements to the election to treat as an expense certain depreciable business assets, and the authorization for a taxpayer to revoke the election at will, do not apply;
- ll) The enhancements to the election to treat certain research and experimental expenditures as a deduction rather than a credit do not apply;
- mm) The transition rule for binding contracts under the limitation on excessive employee remuneration applies to contracts in effect on March 31, 2019;
- nn) The limitation that a "covered employee" be among the five highest compensated employees under the limitation on excessive employee remuneration for taxable years beginning after December 31, 2026 does not apply;
- oo) The imposition and removal of the limitation on the net operating loss deduction for certain taxable years do not apply;
- pp) The definition of taxable income for any such prior taxable year for the purposes of a net operating loss carryback for taxable years beginning after December 31, 2020 does not apply;
- qq) The authorization to taxable years in which a net operating loss may be carried does not apply;

- rr) The special rule for net operating losses arising in certain taxable years does not apply;
- ss) The consideration that a foreign corporation is not a corporation if certain property used in the active conduct of a trade or business is transferred by a U.S. person to a foreign corporation does not apply;
- tt) The carryforward of disallowed business interest, the inclusion of the carryforward as a pre-change loss, and the inclusion of a corporation entitled to the carryforward as a loss corporation do not apply;
- uu) The special rule for application of the energy efficient commercial buildings deduction allowed for corporate real estate investment trusts does not apply;
- vv) The contribution catch-up limits to Individual Retirement Accounts, and to Simple Plans, apply;
- ww) The limitation that the inclusion of an amount as gross income not be later than when accounted for in an applicable financial statement does not apply to certain credit card fees;
- xx) The suspension of the limitation on excess business losses applicable to pass-through entities and sole proprietors, and subsequent extensions, do not apply;
- yy) The treatment of the gain or loss resulting from the disposition of installment obligations by an insurance company does not apply;
- zz) The special rule for federal long-term contracts does not apply;
- aaa) The repeal of the small life insurance company deduction does not apply;
- bbb) The repeal of the deduction for alimony payments made by the payor, and inclusion of the payments in gross income of the recipient, apply on January 1, 2025, as provided, when computing the taxable income of certain estates or trusts;
- ccc) The limitation on like-kind exchanges applies for taxable years beginning on or after January 1, 2025;
- ddd) The basis adjustment for capital gains invested in opportunity zones does not apply;
- eee) The treatment of certain gains by partnership interests held in connection with the performance of services as a short-term capital gain does not apply;
- fff) The exclusion of certain self-created property from the definition of a capital asset does not apply;
- ggg) The rate specified for the withholding of tax on foreign partners' share of effectively connected income is the applicable tax rate under the Revenue and Taxation Code (R&TC);

- hhh) An understatement of gross income resulting from an overstatement of unrecovered cost or other basis is an omission from gross income;
- iii) The penalty for failure to furnish information or maintain records related to certain foreign-owned corporations is \$10,000, rather than \$25,000.
- jjj) Modifications to information returns apply to those filed on or after January 1, 2026;
- kkk) The definition of regular tax under the AMT applies;
- lll) A deduction for the excise tax imposed on the repurchase of corporate stock is prohibited;
- mmm) A deduction for the excise tax imposed on designated drugs during noncompliance period is prohibited;
- nnn) The prohibition on the deduction for any disqualified related party amount paid or accrued in hybrid transactions or with hybrid entities applies;
- ooo) The rate of the imposition of tax on income from prohibited transactions is 100%; and,
- ppp) The 100% exclusion and exception from minimum tax for gains on certain small business stock do not apply.

3) Makes various technical amendments and removes "deadwood" provisions throughout.

**EXISTING LAW** conforms the R&TC to the federal IRC as of January 1, 2015, with certain modifications. Additionally, state law provides for stand-alone provisions that would not generally be impacted by this bill's date change conformity, unless otherwise specified.

**FISCAL EFFECT:** The Franchise Tax Board (FTB) estimates that this bill would result in a revenue gain of more than \$106 million in the 2025-26 fiscal year (FY), \$81 million in FY 2026-27, and \$17 million in FY 2027-28.

#### **COMMENTS:**

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

SB 711 makes it easier for people and businesses to file their taxes by updating R&TC to conform, conform with modification, or not conform to changes that Congress has made to the Internal Revenue Code (IRC) since January 1, 2015. There are more than 1,000 changes the state has not yet acted on, which frustrates taxpaying Californians when they find that state and federal tax laws treat the same issue in opposite ways. This bill is a consensus measure, and implements recommendations intended to conform in a fiscally responsible manner that avoids policy disputes.

2) The California Society of Certified Public Accountants, writing in support of this bill, state, in part:

### **Reduces Complexity and Simplifies Compliance**

When California's tax laws don't align with federal rules, taxpayers and tax practitioners must make numerous adjustments and use different methods to complete their state and federal returns. This added complexity increases the risk of errors and unintentional non-compliance, which can result in costly penalties and interest over time. SB 711 would simplify the process by reducing the number of required adjustments – making tax filing more straightforward and helping taxpayers avoid unnecessary errors and penalties.

### **Eases Administrative Burden**

Non-conformity increases the time, cost, and effort required from taxpayers, tax professionals, and the [FTB]. Taxpayers must maintain separate records for state and federal reporting, while practitioners must make additional adjustments and calculations. The FTB also faces added work verifying returns, conducting audits, and assisting taxpayers. This extra administrative burden adds unnecessary complications and costs to the tax system. SB 711 would streamline reporting and compliance, easing these burdens for everyone involved.

### 3) Committee Staff Comments:

- a) *Conformity in California:* California tax law does not automatically conform to federal tax law changes. 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 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 R&TC in their entirety. In 1983, however, California repealed significant sections of tax law, and replaced them with references to federal 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. AB 154 (Ting), Chapter 359, Statutes of 2015, enacted California's current date-change conformity of January 1, 2015.

- b) *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 the state. 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, give state tax agencies can more often rely on federal audits, case law, and regulations.

These advantages do not come without 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 incent 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, the state 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.

- c) *This bill*: This bill would conform California tax law to the IRC as of January 1, 2025, with certain modifications. This bill maintains non-conformity where California has specifically decoupled from wholesale elements of federal law, such as federal tax credits and their carryover periods. In other areas, this bill would amend certain federal provisions to be appropriate for the state, such as providing a \$10,000 penalty for failure to furnish information for certain foreign-controlled corporations, rather than the federal \$25,000 penalty. Elsewhere, this bill would entirely decouple from certain federal provisions, such as the special rule for federal long-term contracts. Finally, this bill would remove "deadwood" provisions, which is statutory language that references sections of the IRC that have been repealed, and technical amendments to appropriately reference IRC sections that have been renumbered or re-lettered.

The FTB provides a summary of annual changes to federal law, and whether California conforms. Those summaries may be found on the FTB's website, and provide a granular analysis of California conformity to the IRC.

## **REGISTERED SUPPORT / OPPOSITION:**

### **Support**

California Society of Certified Public Accountants  
California Taxpayers Association

### **Opposition**

None on file

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