STATE OF CALIFORNIA
Franchise Tax Board

Bill Analysis

Author: Haney	Sponsor:	Bill Number: AB 1265
	Related Bills: See Legislative History	Introduced: February 21, 2025 Amended: April 10, 2025, and January 5, 2026

SUBJECT

Rehabilitation of Certified Historic Building Credit (Rehabilitation Tax Credit)

SUMMARY

This bill would, under the Personal Income Tax Law (PITL) and Corporate Tax Law (CTL), allow a Rehabilitation Tax Credit for a portion of qualified rehabilitation expenditure with respect to the certified historic structure, not to exceed $5 million per taxpayer.

The bill would also extend the Legislative Analyst Office's (LAO) collaboration with the California Tax Credit Allocation Committee (CTCAC) and the Office of Historic Preservation (OHP) to review the effectiveness of the credit.

This is the Franchise Tax Board's (FTB) first analysis of the bill and only addresses the provisions that would impact the FTB.

RECOMMENDATION

No position—The three-member Franchise Tax Board has not formally voted or taken a position on this bill.

SUMMARY OF AMENDMENTS

The bill, as introduced on February 21, 2025, extended the operative dates of the Rehabilitation Tax Credit to taxable years beginning before January 1, 2031, increased the credit for certain historic structures, and extended the LAO's annual review requirement to January 1, 2031.

The April 10, 2025, amendments redefined "affordable housing for lower income households" and made a nontechnical correction.

The January 5, 2026, amendments removed the amendments related to the Rehabilitation Tax Credit for taxable years beginning on or after January 1, 2021, and before January 1, 2031, added a similar Rehabilitation Tax Credit for taxable years beginning on or after January 1, 2027, and before January 1, 2031, as discussed in this analysis, and extended the requirement that the LAO collaborate with the CTCAC and the OHP to annually review the effectiveness of the credits.

REASON FOR THE BILL

The reason for the bill is to encourage preservation of certified historic buildings.

ANALYSIS

This bill, under the PITL and CTL, would, on an annual basis beginning on January 1, 2027, and until January 1, 2031, extend the requirement that the LAO collaborate with the CTCAC and the OHP to annually review the effectiveness of the credits added by this bill.

This bill would, for taxable years beginning on or after January 1, 2027, and before January 1, 2031, also allow a tax credit to a taxpayer for the rehabilitation expenses of certain homes and historic buildings determined in accordance with federal law (Internal Revenue Code (IRC) section 47). However, in lieu of the amount determined by federal law, the amount of the Rehabilitation Tax Credit for the taxable year would be 20 percent of the qualified rehabilitation expenditures with respect to the certified historic structure, not to exceed $5 million per taxpayer. In addition, the credit would be $0 unless appropriations are provided in a bill related to the Budget Act.

The bill defines the following:

- "Certified historic structure" has the same meaning as defined in IRC section 47(c)(3), that is a structure in this state and is listed on the California Register of Historical Resources.
- "Qualified rehabilitation expenditure" has the same meaning as that term is defined in IRC section 47(c)(2), except that qualified rehabilitation expenditures may include expenditures in connection with the rehabilitation of a building without regard to whether any portion of the building is or is reasonably expected to be tax-exempt use property.
- A qualified rehabilitation expenditure would not have to meet the requirement that it is an expenditure attributable to the rehabilitation of a qualified rehabilitated building that is a certified rehabilitation identified by the Secretary of the Interior.

For a taxpayer to be eligible for the credit, the taxpayer would be required to request a tax credit allocation from the CTCAC in conjunction with OHP by providing necessary information, as determined by the OHP and CTCAC, to obtain the tax credit allocation. A tax credit allocation provided to a taxpayer would not constitute a determination by the CTCAC with respect to the taxpayer's eligibility for the credit.

The bill would require OHP to establish a time period in regulations that a taxpayer who receives a tax credit allocation must begin rehabilitation after the issuance of the tax credit allocation. If the rehabilitation does not begin within the time period established by the OHP, the tax credit allocation would be forfeited and the credit amount associated with the tax credit allocation would be treated as an unused allocation tax credit amount.

This bill specifies that no deduction would be allowed for the same expenses for which the credit was allowed. In addition, if a credit is allowed with respect to any property, the basis of such property would be reduced by the amount of credit allowed. Any credit allowed under this provision would need to be claimed in the first taxable year in which the structure is placed in service.

The unused credit could be carried over eight years, until the credit is exhausted.

The CTCAC would be required to provide the FTB with an annual list of the taxpayers that are allocated a credit, including each taxpayer's identification number and the amount allocated to them.

With regards to the application of the tax credits to entities treated as partnerships for income tax purposes, the credits awarded to a partnership would be allocated to the partners of a partnership in accordance with the partnership agreement, regardless of how the project allocates the federal historic rehabilitation tax credit to its partners or whether the allocation of the credit under the terms of the partnership agreement has substantial economic effect, within the meaning IRC section 704(b). To the extent the allocation of a credit to a partner lacks substantial economic effect, any loss or deduction otherwise allowable under the PITL or CTL that is attributable to the sale or other disposition of that partner's partnership interest made prior to the expiration of the credit's recapture period for the project would not be allowed in the taxable year that the sale or other disposition occurred. Instead, the gain or loss would be deferred until, and treated as if, it occurred in the first taxable year immediately following the taxable year in which the tax credit recapture period ends for the project. The credits awarded to the partnership would be allocated to the partners of that partnership in accordance with the partnership agreement.

The recapture provisions described in IRC section 50(a) would apply when the property (or interest in the property) is sold within the recapture period, which for the federal historic rehabilitation credit is five years from the date the property is placed in service. Twenty percent of the recapture risk decreases each year.

The Rehabilitation Tax Credit could reduce the regular tax plus the tax relating to the separate tax on lump-sum distributions, below tentative minimum tax for taxpayers subject to the PITL and the CTL.

Lastly, the Rehabilitation Tax Credit provisions would remain in effect regardless of the expiration or repeal of IRC section 47, relating to the federal historic rehabilitation credit.

These credits would be repealed on December 1, 2031.

Effective/Operative Date

As a tax levy, this bill would be effective immediately upon enactment and specifically operative for taxable years beginning on or after January 1, 2027, and before January 1, 2031, when the credit is included as an appropriation in the budget.

Federal/State Law

Federal Law

Federal law allows for a historic rehabilitation credit for the rehabilitation of historic buildings. The rehabilitation credit is equal to 20 percent of qualified rehabilitation expenditures. The rehabilitation credit is available to individuals, corporations, partners or shareholders or beneficiaries of a passthrough entity such as a partnership, and estates and trusts.

State Law

For taxable years beginning on or after January 1, 2021, and before January 1, 2027, California allows a similar credit for the rehabilitation expenses of certain homes and historic buildings determined in accordance with federal law (IRC section 47), except as follows:

- The 20 percent general credit for the qualified rehabilitation expenditures of a certified historic structure (other than expenses that qualify for the 25 percent credit below), and
- The 25 percent credit for the qualified rehabilitation expenditures of a certified historic structure if that structure meets any of the following conditions:
    - The rehabilitated structure is located on certain federal surplus property, surplus state real property, or on surplus land.

- The rehabilitated structure includes affordable housing for lower-income households, as defined in Health and Safety Code section 50079.5.
- The structure is located in a designated census tract, as defined in Revenue and Taxation Code (RTC) section 17053.73(b)(7).
- The structure is part of a military base reuse authority, established pursuant to Title 7.86 (commencing with Government Code section 67800).
- The structure is a transit-oriented development that is a higher-density, mixed-use development within a walking distance of one-half mile of a transit station.

Unlike the federal credit:

- The credit is unavailable for expenditures with respect to a qualified building unless it is a certified historic structure.
- The credit is allowed for qualified rehabilitation expenditure amounts for an owner-occupied residence if the expenses are determined to rehabilitate the historic character and improve the integrity of the residence in the year of completion. The Rehabilitation Tax Credit would be allowed for amounts equal to or more than $5,000 but does not exceed $25,000.
- The credit is $0 unless appropriations are provided in a bill related to the Budget Act.
- Certified historic structure has the same meaning as defined in IRC section 47(c)(3) that is a structure in this state and is listed on the California Register of Historical Resources.
- Qualified rehabilitation expenditure has the same meaning as that term is defined in IRC section 47(c)(2), except that qualified rehabilitation expenditures may include expenditures in connection with the rehabilitation of a building without regard to whether any portion of that building is or is reasonably expected to be a tax-exempt use property.
- Qualified rehabilitation expenditure has the same meaning as that term is defined in IRC section 47(c)(2) and also means rehabilitation expenditures incurred by the taxpayer with respect to a qualified residence for the rehabilitation of the exterior of the building or rehabilitation necessary for the function of that home, including, but not limited to, rehabilitation of electrical, plumbing, or foundation of the qualified residence.
- Qualified rehabilitation expenditures would not have to meet the requirement that it is an expenditure attributable to the rehabilitation of a qualified rehabilitated building that is a certified rehabilitation identified by the Secretary of the Interior.

In addition, the following apply:

- No deduction is allowed for an expense for which the credit is allowed, and if a credit is allowed with respect to property, the basis of that property is reduced by the amount of the credit.
- Any unused credit can be carried over for up to eight years.
- The credit can reduce the regular tax plus the tax relating to the separate tax on lump-sum distributions, below tentative minimum tax for taxpayers subject to the PITL and the CTL.
- IRC section 47(c)(1)(B)(ii), relating to special rules for rehabilitation that may be expected to be completed in phases, would not apply.
- The recapture provisions described in IRC section 50(a) apply when the property (or interest in the property) is sold within the recapture period, which for the federal historic credits is five years from the date the property is placed in service. Twenty percent of the recapture risk decreases each year.
- The credit provisions are operative regardless of the expiration or repeal of IRC section 47, relating to the federal rehabilitation credit.

Unlike the federal credit, the entire amount of credit generated can be claimed in the year the building is placed in service.

Current state law requires the LAO, on an annual basis beginning January 1, 2021, through January 1, 2027, to collaborate with the CTCAC and the OHP to review the effectiveness of the credit.

Implementation Considerations

The FTB has identified the following considerations and is available to work with the author's office to resolve these and other considerations that may be identified.

This bill provides that the Legislature intends to comply with the reporting requirements of RTC section 41, however, no reporting requirements are identified. Because the LAO would be required to provide annual reporting, it is recommended that the bill be amended to include the Section 41 requirement language in RTC section 38.10, including when the reporting requirement would expire.

This bill would require an appropriation by the Legislature to pay for the credit. As such, the credits claimed could exceed the amount of appropriated funds and cause the disallowance of the credit for taxpayers.

Technical Considerations

None noted.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

SB 132 (Senate Committee on Budget and Fiscal Review, Chapter 17, Statutes of 2025) under the PITL, beginning on July 1, 2025, requires amounts set aside for certain qualified rehabilitation expenditures under the Rehabilitation Tax Credit not allocated during the 2025 calendar year to be made available within 90 days to taxpayers with qualified rehabilitation expenditures of $1 million or more and that did not receive an allocation of the Rehabilitation Tax Credit, and would have been the next affordable housing project application to receive an award.

SB 711 (McNerney, Chapter 231, Statutes of 2025) under the PITL, CTL, and Administration of Franchise and Income Tax Laws, modified California’s conformity date to the IRC to January 1, 2025, and specified that the changes made by Section 13402(b)(1)(B) of the Tax Cuts and Jobs Act of 2017 (Public Law 115-97) to IRC section 47(c)(2)(B)(iv), relating to qualified rehabilitation expenditures for certified historic structures do not apply.

AB 150 (Assembly Committee on Budget, Chapter 82, Statutes of 2021), among other things, extended the operative date of the Rehabilitation Tax Credit for qualified rehabilitation expenditures under the PITL and the CTL to taxable years beginning before January 1, 2027. In addition, the bill extended the collaboration period between the CTCAC and the OHP to January 1, 2027, and added specific Section 41 goals and performance metrics for the credit.

SB 451 (Atkins, Chapter 703, Statutes of 2019) created the Rehabilitation Tax Credit for historic rehabilitation expenses that, under the PITL and the CTL, is available for allocation, upon appropriations, by the CTCAC for calendar years 2021 through 2026. In addition, this bill added specific Section 41 goals and performance metrics.

PROGRAM BACKGROUND

None noted.

OTHER STATES’ INFORMATION

None noted.

FISCAL IMPACT

FTB's costs to implement this bill have yet to be determined. As the bill moves through the legislative process, costs will be determined.

ECONOMIC IMPACT

Revenue Estimate

This bill would result in the following revenue loss:

Estimated Revenue Impact of AB 1265 as Amended January 5, 2026
Assumed Enactment After June 30, 2026

($ in Millions)

Fiscal Year	Revenue*
2026-2027	-$0
2027-2028	-$1.1
2028-2029	-$4.3

*This estimate assumes appropriations related to the Budget Act would fully allocate funds to this credit. In addition, credits allocated cannot be used until the building has been placed into service. As a result, credit usage would begin in 2028 and increase each year thereafter.

This analysis does not account for changes in employment, personal income, or gross state product that could result from this bill or for the net final payment method of accrual.

Revenue Discussion

Based on data from the OHP and the California State Park, it is estimated that the total qualified rehabilitation expenditures would be $130 million in taxable year 2027. Applying the 20 percent credit rate and the annual cap of $5 million per taxpayer results in credits generated of $26 million in 2027.

Because allocated credits cannot be used until the building is placed in service, the revenue loss does not begin until the 2028 taxable year. It is estimated that approximately $2.3 million in credit would be used by taxpayers in the 2028 taxable year and that amount would increase over time peaking at an estimated revenue loss of about $17 million in the 2031 taxable year.

The tax year estimates are converted to fiscal year estimates and then rounded to arrive at the amounts reflected in the above table.

LEGAL IMPACT

None noted.

EQUITY IMPACT

None noted.

APPOINTMENTS

None noted.

SUPPORT/OPPOSITION

To be determined.

ARGUMENTS

To be determined.

LEGISLATIVE CONTACT

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