



Bill Analysis

Author: Haney

Sponsor:

Bill Number: AB 1869

Related Bills: See Legislative
History

Introduced: February 12, 2026

SUBJECT

Real Estate Investment Trusts' (REIT) Management Activities

SUMMARY

Effective January 1, 2027, this bill would, under the Corporate Tax Law (CTL), amend the definition of "rents from real property" to specifically state that certain activities are operating and managing activities for purposes of determining impermissible tenant service income (ITSI), and would allow employees of lodging facilities to report evidence to the Franchise Tax Board (FTB) that a REIT or its subsidiary is operating or managing the facility.

RECOMMENDATION

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

SUMMARY OF AMENDMENTS

Not applicable.

REASON FOR THE BILL

The reason for the bill is to specify that certain activities by a REIT are deemed operating and managing in connection with a lodging facility for purposes of qualifying as ITSI and to allow employees to report potential ITSI activities to the FTB.

ANALYSIS

This bill would, under the CTL, for purposes of inclusion of rents from real property in the income of the REIT, amend the definition of ITSI by including within operating and managing the following activities by a REIT in connection with a lodging facility:

- Exercising control over wages, hours, or working conditions of employees at a lodging facility.
- Exercising control over the discretion of another entity, including an eligible independent contractor as defined in Section 856(d)(9)(A) of the Internal Revenue Code, to establish any aspect of the wages, hours, or working conditions of employees at the lodging facility.

- Exercising, or reserving the right to exercise, control over the negotiation, approval, or application of any collective bargaining agreement covering employees at the lodging facility.

This bill would provide that the inclusion of the specified activities by a REIT in connection with a lodging facility in the definition of ITSI, is declaratory of existing law.

This bill would also require the FTB to receive evidence submitted by an affected employee at a lodging facility, or their representative, that a REIT or taxable REIT subsidiary is directly or indirectly operating or managing a lodging facility, and to confirm receipt and provide a written response within the bill's unspecified timeframe.

Effective/Operative Date

This bill would be effective and operative January 1, 2027.

Federal/State Law

Federal Law

In general

REITs are structured as entities that meet specific organization requirements and are generally restricted to those entities investing in passive investments, primarily in real estate and securities.

A REIT must satisfy four conditions on a year-by-year basis: organizational structure, source of income, nature of assets, and distribution of income. Whether the REIT meets the asset conditions is generally measured each quarter.

Organizational structure requirements

To qualify as a REIT, an entity must be for its entire taxable year, a corporation or an unincorporated trust or association that would be taxable as a domestic corporation if the REIT provisions were unavailable, and must be managed by one or more trustees. Except for the first taxable year when an entity elects to be a REIT, the beneficial ownership of the entity must be held by 100 or more persons, and the entity may not be so closely held by individuals that it would be treated as a personal holding company if all its adjusted gross income constituted personal holding company income. A REIT is required to comply with regulations to ascertain the actual ownership of the REIT's outstanding shares.

Income requirements

For an entity to qualify as a REIT, at least 95 percent of its gross income generally must be derived from certain passive sources (the "95 percent income test"). In addition, at least 75 percent of its income generally must be from certain real estate sources (the "75 percent income test"), including rents from real property (as defined) and gain from the sale or other disposition of real property, and income and gain derived from foreclosure property.

Rents from real property do not include any ITSI. ITSI means, with respect to any real or personal property, any amount received accrued directly or indirectly by the REIT for services furnished or rendered by the trust to the tenants of such property, or managing or operating such property. If ITSI from a property exceeds 1 percent of the total amounts received or accrued for that property during the taxable year, all income from such property is treated as other than rents from real property.

State Law

REITS

California generally conforms to federal REIT rules as of the specified date of January 1, 2025, with modifications. However, California law provides that a corporation, trust, or association that is a REIT for any taxable year for federal purposes is automatically a REIT for California purposes for the same taxable year. Conversely, a corporation, trust, or association that is not a REIT for any taxable year for federal purposes is automatically not a REIT for California purposes for the same taxable year.

Tax Fraud/Tax Enforcement

Under state law, the FTB is responsible for administering and enforcing the franchise and income tax laws under the Revenue and Taxation Code, including the identification and resolution of tax fraud (the intentional underreporting or failing to report income). In general, the FTB's enforcement activity includes the audit, protest, appeals, filing enforcement, collection, and criminal investigation programs. However, information on alleged tax fraud by an individual or business, including whistleblower complaints, can be submitted to the FTB by phone, fax, mail, or online.

Privacy and Disclosure

State law prohibits the disclosure of any confidential taxpayer information, except as specifically authorized by statute. Any FTB employee or member responsible for the unauthorized disclosure of state or federal tax information is subject to criminal prosecution. Improper disclosure of state tax information is a misdemeanor and improper disclosure of federal tax information is a felony. Similarly, the prohibition also includes the disclosure to an authorized recipient of confidential taxpayer data.

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 uses undefined terms, e.g., "affected employees," "representative," and "__days of receipt." The absence of definitions and specified days could lead to taxpayer confusion. For clarity, the author may wish to amend the bill to define these terms.

Technical Considerations

For consistency in terminology, the following changes are recommended:

- In Section 24872.4(c)(1)(A), replace "impermissible tenant service income," with "in general,".
- In Section 24872.4(c)(1)(A), add, "relating to exceptions," after "Section 856(l)(3)(A) of the Internal Revenue Code,".
- In Section 24872.4(c)(1)(A)(ii), add, "relating to in general," after "Internal Revenue Code,".

Policy Considerations

California generally conforms to the definition of rents from real property, which is used to determine whether an entity qualifies as a REIT. In addition, an entity that is a REIT for federal purposes is a REIT for California purposes. This provision would identify specific operating and managing activities that would be excluded from being considered rents from real property for California purposes, which could impact whether an entity is considered a REIT for California purposes. This could create difficulty for taxpayers if it results in an entity being considered a REIT for federal purposes and not for California purposes.

LEGISLATIVE HISTORY

No legislation similar to this bill has been identified.

PROGRAM BACKGROUND

Information received, generated, and maintained by the FTB is generally considered confidential unless specifically provided otherwise by statute. The FTB has stringent departmental policies and procedures regarding privacy and disclosure. All employees receive training annually about ensuring the confidentiality of taxpayer information and are given updated procedures on a regular basis. Any violation of these policies and procedures is subject to disciplinary action, punishable by law, or both.

The California Public Records Act provides access to public information the FTB maintains unless the records are exempt from disclosure by law. This may include written or electronic information.

The FTB is exempt from disclosing certain types of information, such as:

- Personnel, medical, or similar files for FTB employees.
- Test questions and scoring keys for employment exams.
- Preliminary drafts of documents not retained by the FTB.
- Records pertaining to pending litigation.
- Confidential tax return information.

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 as introduced February 12, 2026, would not impact the computation of state income or franchise tax.

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.

LEGAL IMPACT

None noted.

EQUITY IMPACT

None noted.

APPOINTMENTS

None noted.

SUPPORT/OPPOSITION

To be determined.

ARGUMENTS

To be determined.

LEGISLATIVE CONTACT

FTBLegislativeServices@ftb.ca.gov