STATE OF CALIFORNIA
Franchise Tax Board

# Bill Analysis

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| Author: Hurtado | Sponsor: | Bill Number: SB 1287 |
| | Related Bills: See Legislative History | Introduced February 20, 2026, and Amended April 9,2026 |

## SUBJECT

Shortline Railroad Modernization Act of 2026

## SUMMARY

This bill would, under the Personal Income Tax Law (PITL) and Corporation Tax Law (CTL), create the Shortline Railroad Modernization Act of 2026 (Act). This Act would provide two tax credits for qualified taxpayers, (1) for qualified shortline railroad expenditures for taxable years beginning on or after January 1, 2027, and before January 1, 2032, and (2) for qualified new rail infrastructure expenditures for taxable years beginning on or after January 1, 2028, and before January 1, 2033.

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

## RECOMMENDATION

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

## SUMMARY OF AMENDMENTS

The April 9, 2026, amendments added separate sunset and repeal dates for each tax credit, modified the definition of a "qualified taxpayer", "qualified shortline railroad expenditures", "qualified new rail infrastructure expenditures" and "new rail infrastructure project." The amendments also removed the assignment of the tax credit provisions, added sale of the tax credit provisions, modified the Revenue and Taxation Code (RTC) section 41 reporting requirements, and modified provisions related to credit certification.

## REASON FOR THE BILL

The reason for the bill is to facilitate the modernization of shortline railroad infrastructure and build new rail connections by creating two new tax credits.

ANALYSIS

This bill would, under the PITL and CTL, create the Shortline Railroad Modernization Act of 2026 (Act). This Act would also provide the following two tax credits to qualified taxpayers.

*The Qualified Shortline Railroad Expenditures Tax Credit*

This bill would, under the PTIL and CTL, for taxable years beginning on or after January 1, 2027, and before January 1, 2032, provide a tax credit equal to 50% of qualified shortline railroad expenditures. The amount of the tax credit allowed cannot exceed the product of $5,000 and the number of miles of railroad track owned or leased within the State of California by the qualified taxpayer at the close of the taxable year for which the credit is claimed. In addition, the aggregate amount of credit that may be allocated in a fiscal year for qualified shortline railroad expenditures cannot exceed $7,000,000.

In order for a taxpayer to be allocated this tax credit, a taxpayer must be issued a credit certificate by the Department of Transportation (Department). The taxpayer must submit an application, in the form and manner as prescribed by the Department, for qualified shortline railroad expenditures incurred.

The Department would evaluate the taxpayer's application and issue a credit certificate upon determining the taxpayer meets the criteria.

The Department would then issue a credit certificate on a first come first serve basis subject to the $7,000,000 aggregate amount limitation per fiscal year. The issued credit certificate would state the amount of credit allocated to the qualified taxpayer.

In addition, the Department is required to annually provide the FTB with a list of qualified taxpayers that were issued a credit certificate and the amount of tax credit allocated to each qualified taxpayer. This bill would also allow the FTB to disallow the credit to a taxpayer that received a credit certification from the Department if the FTB finds that the taxpayer does not meet the criteria provided in this bill.

For purposes of this tax credit, the bill defines the following terms:

"Qualified Taxpayer" is a person or entity engaged in a trade or business that operates a railroad located wholly or partly in California that is classified by the federal Surface Transportation Board as a Class II or Class III railroad.

"Qualified shortline railroad expenditures" means the following:

- Nonreimbursed costs paid or incurred by the qualified taxpayer for railroad infrastructure maintenance or capital improvements of infrastructure or capital owned or leased by the qualified taxpayer to operate a Class II or Class III railroad, including, but not limited to, maintenance of or improvements to rail, tie plates, joint bars, fasteners, switches, ballast, subgrade, bridges, industrial leads, sidings, signs, safety barriers, crossing signal and gates, industrial spur, industry track and related track structures.
- Does not include any cost paid or incurred by the qualified taxpayer that is used as the basis for a federal tax credit that is funded by a federal grant or that was paid or incurred more than 12 months before the date the qualified taxpayer submitted their application for the credit certification.

The unused credit could be carried over for six years until exhausted. Any deduction or credit otherwise allowed for qualified expenditures made by the qualified taxpayer as a trade or business expense would be reduced by the amount of this credit allowed. In addition, a qualified taxpayer may sell any credit allowed under the provisions of this bill.

Lastly, the FTB may prescribe rules, guidelines, or procedures necessary or appropriate to carry out the provisions of the credits.

The credit would be repealed on December 1, 2032.

*The Qualified New Rail Infrastructure Expenditures Tax Credit*

This bill would, under the PITL and CTL, for taxable years beginning on or after January 1, 2028, and before January 1, 2033, allow a tax credit equal to 50% of qualified new rail infrastructure expenditures. The amount of tax credit allowed cannot exceed $1,000,000 per new rail infrastructure project completed in the taxable year for which the credit is claimed. In addition, the aggregate amount of credit that may be allocated in a fiscal year for qualified new rail infrastructure expenditures cannot exceed $10,000,000.

In order for a taxpayer to be allocated this tax credit, a taxpayer must be issued a credit precertification letter and a credit certificate by the Department. For a taxpayer to apply for a precertification letter, the taxpayer must submit an application, in form and manner as prescribed by the Department, for credit precertification.

Beginning January 1, 2027, and before January 1, 2033, the Department would establish a quarterly application window for precertification applications. The Department will review the taxpayers' application and will issue a credit precertification letter upon determining the project and the taxpayer meets all the criteria.

The allocation of this credit is subject to the $10,000,000 aggregate amount limitation per fiscal year. If the annual aggregate amount is not fully allocated in any quarterly period, the unused amount would be carried forward to the next quarterly application period within the same fiscal year. Any amount not awarded by the close of the fiscal year shall expire.

The credit precertification letters would include a maximum amount of the credit that is allowed and based on the estimated new rail infrastructure expenditures included in the application.

The qualified taxpayer would then be required to submit an application annually, in the form and manner as prescribed by the Department, to provide any documentation, related to their qualified expenditures incurred for the new rail infrastructure project, to allow the Department to determine whether the taxpayer has incurred qualified new rail infrastructure expenditures as submitted in their application for which a credit precertification letter was issued.

The Department would then review the taxpayer's application and issue a credit certificate once they determine the taxpayer qualifies.

The credit certificate would state the amount of the credit allowed for the taxable year for which the annual certification application was received and the remaining amount of the credit allocated pursuant to the precertification letter. The amount of the credit cannot exceed the maximum amount listed on the taxpayer's credit precertification letter.

This bill would also allow the FTB to disallow a credit to a taxpayer that received a credit certification from the Department if the FTB finds that the taxpayer does not meet the criteria provided in this bill.

In addition, the Department would be required to annually provide the FTB with a list of qualified taxpayers that receive a certificate, the allocated tax credit amounts per taxpayer, any remaining credit amounts pending to be allocated on the precertification letters, and any other information FTB deems necessary to administer the credit.

For purposes of this tax credit, the bill defines the following terms:

"Qualified Taxpayer" is either a person or entity engaged in a trade or business that operates, or a company that owns a railroad located wholly or partly in California that is classified by the federal Surface Transportation Board as a Class II or Class III railroad or an owner or lessee of a rail siding, industrial spur, or industry track located on or adjacent to any railroad in California. Under this provision a qualified taxpayer does not include a railroad that is classified by the federal Surface Transportation Board as a Class I railroad.

"Qualified new rail infrastructure expenditures" would mean the following:

- Nonreimbursed costs paid or incurred by the qualified taxpayer for a new rail infrastructure project that has been pre-certified by the Department and commenced within 12 months of the issuance of a credit precertification letter.
- Does not include any costs paid or incurred by the qualified taxpayer that is used as the basis for a federal tax credit, that is funded by a federal grant, or that was paid or incurred more than 12 months before the date the qualified taxpayer submitted their application for credit certification.

"New rail infrastructure project" would mean a project to construct new rail infrastructure, or improvements thereto, included with servicing customer locations or expansions by any railroad located in California, including, but not limited to, a right-of-way; new track, including industrial leads, switches, spurs, and siding; rail loading dock; and transloading structures.

The unused credit could be carried over for six years until exhausted. Any deduction or credit otherwise allowed for qualified expenditures made by the qualified taxpayer as a trade or business expense would be reduced by the amount of this credit allowed. In addition, a qualified taxpayer may sell any credit allowed under the provisions of this bill.

Lastly, the FTB may prescribe rules, guidelines, or procedures necessary or appropriate to carry out the provisions of the credits.

The credit would be repealed on December 1, 2033.

*RTC Section 41 Requirements*

The bill includes RTC section 41 reporting requirements that would provide that the measurement of the effectiveness of the credits achieving their intended goals would include key performance indicators, including:

- The number of miles of railroad track improved, rehabilitated, or constructed
- The number and types of rail infrastructure projects completed, such as track, bridges, sidings, and spurs; and
- The amount of private capital investment leveraged, measured as the ratio of private dollars invested per tax credit dollar claimed.

Data collection requirements to determine the effectiveness of the credit must include the following:

- A description of the project, its location, the general scope of work, and, when applicable, the approximate miles of track improved or constructed.
- The amount of qualified expenditures incurred and the total credit claimed.

This bill would also require the Department, in collaboration with the FTB, to submit a report to the Legislature on or before June 30, 2028, and each June thereafter. The RTC section 41 reporting requirements would be treated as an exception to the general prohibition against disclosure of confidential taxpayer information.

*Effective/Operative Date*

As a tax levy, this bill would be effective immediately upon enactment. The qualified shortline railroad expenditures tax credit would specifically be operative for taxable years beginning on or after January 1, 2027, and before January 1, 2032, and the qualified new rail infrastructure expenditures tax credit would specifically be operative for taxable years beginning on or after January 1, 2028, and before January 1, 2033.

*Federal/State Law*

*Federal Law*

Existing federal law provides a Qualified Railroad Track Maintenance Credit which is equal to 40 % (50% in the case of any taxable years beginning before January 1, 2023) of the qualified railroad track maintenance expenditures paid or incurred by an eligible taxpayer. The amount of the credit is limited to $3,500 multiplied by the sum of the number of miles of railroad track owned or leased by the eligible taxpayer as of the close of the taxable year, and the number of miles of railroad track assigned to the taxpayer by a Class II or Class III railroad which owned such track. The term "Qualified Railroad Track Maintenance Expenditures" is defined as gross expenditures (whether or not otherwise chargeable to capital account) for maintaining railroad track, including roadbed, bridges, and related track structures, owned or leased as of January 1, 2015, by a Class II or Class III railroad. In addition, the basis of such tracks is required to be reduced by the amount of credit allowed.

*State Law*

There is no comparable state income tax credit similar to the credits this bill would create.

*Implementation Considerations*

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

Typically, credits involving areas for which the FTB does not have the expertise are certified by another agency that has the relevant expertise. The certification language should specify the responsibilities of both the certifying agency and the taxpayer. It is recommended that this bill be amended to remove the provisions allowing FTB to disallow a credit based on criteria used by the Department. It is important to ensure that only the Department is responsible for evaluating and certifying the tax credits and that the Department is responsible for providing the FTB with any information related to a taxpayer no longer qualifying for the tax credits.

The bill includes a precertification process and a credit certification process. For clarity, the author may wish to specify whether the total amount of the credit allocated in the precertification process must be claimed in the same taxable year under the same credit certification application, or whether the precertification amount may be claimed in multiple taxable years with multiple credit certification applications. The author may also wish to clarify whether the aggregate amount of the credit allowed in Section 17053.32(a)(2) and 23632(a)(2) applies to the total precertification allocation or to each taxable year the credit is claimed if the precertification amount is claimed over multiple taxable years.

The bill, as currently drafted, provides that notwithstanding any other law, a qualifying taxpayer may sell any credit allowed to an unrelated party. However, the bill does not specify the procedures governing the sale of the tax credit. It is recommended that the bill be amended to include clear guidance on the process for selling the credit, including any required documentation, administrative steps, and timeline.

*Technical Considerations*

For consistency and clarity, the following changes are recommended:

- In Section 17053.31(b)(3)(A) replace the phrase "to operate a Class II or Class III railroad" with "to operate a railroad that is classified by the federal Surface Transportation Board as a Class II or Class III railroad".
- In Section 17053.31(h)(2)(C) replace the phrase "tax credit claimed" with "tax credit allowed".
- In Section 17053.31(h)(3)(A) replace the phrase "project for which the credit was claimed" with "project for which the credit was allowed".
- In Section 17053.31(h)(3)(B) replace the phrase "credit claimed" with "credit allowed".
- In Sections 17053.31(a)(3), 17053.32(a)(3), 23631(a)(3), and 23632(a)(3), replace "subdivision (d)" with "subdivision (f)."
- In Sections 17053.31(g), 17053.32(g), 23631(g) and 23632(g) strike out (g) entirely as it is unnecessary language because the FTB would have the authority to prescribe rules and regulations under general provisions.

- In Sections 17053.31(f)(2), 17053.31(h)(3)(B), 23631(f)(2), and 23632(f)(3) replace the term "incurred" with "paid or incurred".
- In Sections 17053.31(b)(3)(A), 17053.32(b)(4)(A), 23631(b)(3)(A) and 23632(b)(4)(A) replace the term "nonreimbursed" with "unreimbursed".

Replace the terms "board" with "Franchise Tax Board" and "department" with "Department of Transportation" throughout the bill. The terms "board" and "department" are generally used to mean the California Board of Equalization and California Department of Tax and Fee Administration throughout the RTC. To avoid taxpayer confusion, it is recommended author amend the bill.

If consistent with the author's intent, the bill could be amended to replace the undefined terms company, entity, and person in the definitions of qualified taxpayer throughout the bill with the term "taxpayer," which is a defined term in the RTC.

For consistency within the RTC and ease of administration, the language in each subdivision (d) throughout the bill should be replaced with "(d). If the credit allowed by this section is claimed by the qualified taxpayer, a deduction otherwise allowed under this part for any amount of qualified [shortline railroad or new rail infrastructure] expenditures paid or incurred by the qualified taxpayer shall be reduced by the amount of the qualified [shortline railroad or new rail infrastructure] expenditures taken into account in calculating the credit allowed by this section."

*Policy Considerations*

This credit would be allowed for 50% of qualified shortline railroad expenditures paid or incurred either inside or outside of California. If this is contrary to the author's intent, the author may wish to amend the bill.

The bill requires the Department in collaboration with the FTB to report on the performance of the credit allowed by this bill on or before June 30, 2028, and each June 30 thereafter. For a report that contains complete information for the 2027 taxable year, it is recommended that the reporting due date be extended to June 30, 2029. If the reporting due date remains unchanged, the report would include the information available as of six months prior to the report due date, which would exclude taxpayer information for those filing both on time and on extension.

For clarity, the author may want to amend the bill to specify that the credit is allowed for expenses paid or incurred *in the taxable year*.

LEGISLATIVE HISTORY

SB 667 (Archuleta, 2025/2026) would, under the Public Utilities Code, require certain railroads, including those operating at speeds above 10 miles per hour, to install wayside detector systems. SB 667 is currently in the Assembly Committee process.

SB 87 (Hurtado, Chapter 32, Statutes of 2019) provided, under the Government Code, a competitive funding program for short-line railroad infrastructure projects and included a one-time appropriation of $7.2 million for the program from the commissioner's Trade Corridors Improvement Fund.

AB 1397 (Burke, 2019/2020) would have, under the PITL and CTL, for taxable years beginning on or after January 1, 2020, and before January 1, 2025, allowed a tax credit of 50% of the qualified taxpayer's qualified railroad reconstruction or replacement expenditures. The amount of credit would have been limited to $3,500 multiplied by the number of miles of railroad track owned or leased within the state by the qualified taxpayer at the taxable year end. AB 1397 did not pass out of the Assembly by the required deadline.

PROGRAM BACKGROUND

None noted.

**OTHER STATES' INFORMAT**ION

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 SB 1287 as Amended April 9, 2026
Assumed Enactment after June 30, 2026

($ in Millions)

| Fiscal Year | Revenue |
|---|---|
| 2026-2027 | -$1.6 |
| 2027-2028 | -$7.0 |
| 2029-2030 | -$11 |

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 federal data, it is assumed that annual expenditures on both the qualified railroad track maintenance and expenditures on new rail infrastructure projects would be large enough to reach the annual aggregate credit caps of $7 million and $10 million respectively, as provided by the bill.

For tax year 2027, the credit for qualified shortline railroad expenditures is estimated to be $7 million. It is estimated that 90%, including the S corporation adjustment, or $6.3 million, would be earned by taxpayers with sufficient tax liability to offset with the credit. Of that amount 60%, or $3.8 million, would be claimed in the year generated and the remaining credit would be used over the subsequent six years or until exhausted.

To arrive at the offsetting tax effect of the expense deduction that would otherwise be allowed under current law, it is estimated that qualified taxpayers would be able to deduct approximately $3.8 million in qualified expenses in taxable year 2027. Applying an average tax rate of 6%, results in an offsetting revenue gain of $250,000. The resulting net revenue loss, for taxable year 2027, would be $3.5 million relating to the qualified shortline railroad expenditures. For taxable year 2028, it is assumed that approximately $9.6 million in credit would be used relating to the qualified shortline railroad expenditures and the qualified new rail infrastructure expenditures.

The tax year estimates are converted to fiscal year revenue estimates, rounded and reflected in the above table.

LEGAL IMPACT

None noted.

EQUITY IMPACT

None noted.

APPOINTMENTS

None noted.

SUPPORT/OPPOSITION

Senate Committee on Transportation, date April 17, 2026

*Support*

- California Short Line Railroad Association (Co-Sponsor)
- Genesee & Wyoming Railroad Services, INC. (Co-Sponsor)
- Arizona & California Railroad Company
- Association of California Egg Farmers
- California Grain & Feed Association
- California Northern Railroad Company
- Central Oregon & Pacific Railroad INC.
- Central Valley Ag Group
- City of Oakdale
- Huron Transfer, LLC
- JS West and Companies
- Pacific Egg & Poultry Association
- Patriot Rail
- Quality Transport, Inc & Trucking-rail Handling, INC.
- San Diego & Imperial Valley Railroad Company, INC.
- San Joaquin Valley Policy Council
- Sierra Northern Railway
- Titan Terminal and Transport
- Tuolumne County Transportation Council
- Ventura County Railroad Company
- Ventura Transfer Company

*Opposition*

- California Tax Reform Association

ARGUMENTS

Senate Committee on Transportation, date April 17, 2026

*Proponents*

None of file.

*Opponents*

Writing in opposition of this bill, the California Tax Reform Association, in part:

> "We do not believe that the use of tax credits is the appropriate way to further the development of short-line railroads. Rather...a direct grant program, authorized through the budget process, is less complex and likely to be more helpful."

LEGISLATIVE CONTACT

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