STATE OF CALIFORNIA
Franchise Tax Board

Bill Analysis

Author: Grayson

Sponsor:

Bill Number: SB 587

Related Bills: See Legislative History

Amended: May 7 and May 23, 2025

SUBJECT

Credit for Local Portion of Sales Tax Reimbursement or Use Tax Paid for Manufacturing and Research and Development (R&D) Equipment

SUMMARY

This bill would, under the Personal Income Tax Law (PITL) and the Corporation Tax Law (CTL), allow taxpayers an income tax credit equal to the non-exempt portion of sales tax reimbursement or use taxes paid during the taxable year on the purchase of, or the storage, use, or other consumption in this state, of certain qualified tangible personal property (TPP), related to manufacturing, R&D, or the generation and production of electrical power for taxable years beginning on or after January 1, 2026, and before January 1, 2031.

RECOMMENDATION

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

SUMMARY OF AMENDMENTS

The May 7, 2025, amendments modified the bill repeal date, extended the Section 41 reporting date, and made other technical changes. These amendments resolved the implementation consideration, and one of two technical considerations discussed in the Franchise Tax Board's (FTB) analysis of the bill as amended March 24, 2025, and created a new technical consideration.

The May 23, 2025, amendments added appropriation language for the administration of this credit and a reporting requirement for the Department of Finance (DOF).

REASON FOR THE BILL

The reason for the bill is to incentivize growth in manufacturing and R&D in California.

ANALYSIS

For taxable years beginning on or after January 1, 2026, and before January 1, 2031, this bill would, under the PITL and the CTL, allow a taxpayer a credit against net tax in an amount equal to sales tax reimbursement or use taxes paid on certain gross receipts during the taxable year for the following sales and use taxes that would be exempt under Revenue and Taxation Code (RTC) section 6377.1, but for RTC section 6377.1(d):

- Sales and use taxes levied by a county, city, or district under either the Bradley-Burns Uniform Local Sales and Use Tax Law or the Transactions and Use Tax Law.
- Sales and use taxes that are credited to the Local Revenue Fund, the Local Revenue Fund 2011, or the Local Public Safety Fund.

The credit would be applicable only for the sales tax reimbursement or the use taxes paid on gross receipts for qualified TPP used for specified purposes including manufacturing, R&D, maintenance of TPP used for manufacturing and R&D, and TPP used in electric power generation or production or electric power storage and distribution, and other purposes.

This bill would, by reference to Section 6377.1, incorporate that section’s definitions.

In addition, the bill provides that a deduction for an amount upon which the credit is based would be reduced by the amount of the credit.

Any unused credit could be carried over for up to 9 years, until exhausted.

The credit could only be claimed on a timely filed original return of a taxpayer.

A credit, or a credit carryover, would not be allowed and the taxpayer would be required to file an amended return if a credit was claimed, with respect to qualified TPP if within one year from the date of purchase the TPP was:

- Removed from California,
- Converted from an exempt use under Section 6377.1(a) to some other use not qualifying for exemption, or
- Used in a manner not qualifying for exemption.

This bill would allow the FTB to request any information necessary for the administration of this credit from the California Department of Tax and Fee administration (CDTFA) and allow CDTFA to provide information to the FTB in a form and manner agreed upon by the CDTFA and the FTB, regarding the exemption claimed pursuant to Section 6377.1.

The FTB would be allowed to prescribe rules, guidelines, procedures, or other guidance to implement this bill. The Administrative Procedures Act would not apply to rules, guidelines, or procedures prescribed by FTB for this bill. The FTB would also be allowed to adopt regulations necessary or appropriate to implement this bill, including regulations to prevent improper claims from being filed.

The bill includes, for purposes of complying with Section 41, the Legislature's findings and declarations that are:

- The goal, purpose, and objective of this credit is to encourage new and continued investment in California in the areas of manufacturing and R&D.
- Detailed performance indicators for the Legislature to use in determining whether the credit meets the goal, purpose, and objective are as follows:
    - The total dollar amount of tax credits allowed.
    - The number of taxpayers that are allowed a credit.

This bill would require the FTB, on or before April 1, 2033, to provide to the Legislature a report on the total dollar amount of credits allowed and the number of taxpayers allowed the credit.

The Section 41 reporting requirements would be treated as an exception to the general prohibition against disclosure of confidential taxpayer information.

This credit would only be allowed for taxable years for which the Legislature appropriates money in the Budget Act for the administration of the credits established by this bill.

This credit would be in effect only until December 1, 2031, and would be repealed on January 1, 2034.

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, 2026, and before January 1, 2031, contingent on the Legislature appropriating money in the Budget Act for the administration of the credits established by this bill.

Federal/State Law

Federal Law

No comparable provision in federal law.

State Law

Under RTC section 6377.1, a partial sales and use tax exemption is allowed for qualified TPP used primarily in one of the following activities:

- Any stage of the manufacturing, processing, refining, fabricating, or recycling process.
- R&D.
- To maintain, repair, measure, or test any qualified TPP used for manufacturing and R&D.
- The generation or production, storage or distribution of electric power.
- For use by a contractor purchasing that property for use in the performance of a construction contract for a qualified person, provided that the qualified person will use the resulting improvement to real property as an integral part of the manufacturing, processing, refining, fabricating, or recycling process, the generation or production, storage or distribution, of electric power, or as a research or storage facility for use in connection with those processes.
- A qualified person is someone who is engaged primarily in the business of manufacturing or electric power generation or distribution.

The exemption is limited to $200 million in qualified TPP purchases annually.

However, the partial exemption does not currently apply with respect to the following sales and use taxes:

- Sales and use taxes levied by a county, city, or district under either the Bradley-Burns Uniform Local Sales and Use Tax Law or the Transactions and Use Tax Law.
- Sales and use taxes that are credited to the Local Revenue Fund, the Local Revenue Fund 2011, or the Local Public Safety Fund.

Implementation Considerations

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 credit would be contingent upon an appropriation for the administration of the credit in the annual Budget Act or another statute, which could create uncertainty for taxpayers, tax preparers, software providers, and the FTB. In addition, uncertainty may reduce the incentive for taxpayers to invest in qualified TPP. If this is not the intent, the author may want to amend the bill.

Technical Considerations

The first sentence of Sections 17053.90(h)(1) and 23623(h)(1) and Sections 17053.90(h)(2) and 23623(h)(2) provide language, relating to guidance and regulations, that are unnecessary. The author may wish to amend this bill to remove this language.

Sections 17053.90(i)(2) and 23623(i)(2) should be standalone subdivisions of the bill since the paragraphs are not specific to subdivision (i).

Policy Considerations

None noted.

LEGISLATIVE HISTORY

AB 52 (Grayson, 2023/2024), similar to this bill, would have, under the PITL and the CTL, allowed taxpayers an income tax credit for the non-exempt portion of sales tax reimbursement or use taxes paid during the taxable year on the sale of, or the storage, use, or other consumption in this state of certain qualified TPP, related to manufacturing, R&D, or the generation and production of electrical power. This bill was vetoed by Governor Newsom noting:

> As a strong supporter of California's innovation economy and manufacturing sector, I agree with the intent of this bill. California offers many powerful incentives to encourage new and continued investment in the areas of manufacturing, research, and development. However, by enacting a new tax credit, this bill would have a significant impact on the state general fund, and should be considered in the annual budget process.
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> In partnership with the Legislature this year, my Administration has enacted a balanced budget that avoids deep program cuts to vital services and protected investments in education, health care, climate, public safety, housing, and social service programs that millions of Californians rely on. It is important to remain disciplined when considering bills with significant fiscal implications that are not included in the budget, such as this measure.

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 SB 587 Amended on May 23, 2025
Assumed Enactment after June 30, 2025

($ in Millions)

Fiscal Year	Revenue*
2025-2026	-$50
2026-2027	-$210
2027-2028	-$330

*This estimate assumes that an appropriation in the Budget Act for the administration of the credit will be made each taxable year the bill is operative.

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 DOF and CDTFA, it is estimated qualified taxpayers would spend approximately $12 billion on qualified purchases in 2026. It is expected taxpayers would pay approximately $490 million of qualified taxes on these purchases resulting in credits generated of $490 million in the 2026 taxable year. It is estimated approximately 5 percent of taxpayers would not qualify for the credit either because they moved the property out of the state within one year from the date of purchase or would not claim the credit on a timely filed original return, thus reducing total credits to $460 million. It is assumed that 45 percent, including the S corporation adjustment and business credit limitation added by Senate Bill 167 (Senate Committee on Budget and Fiscal Review, Chapter 34, Statutes of 2024), or $220 million, would be earned by taxpayers with sufficient tax liability to offset the credit in 2026. Of that amount 60 percent, or $140 million, would be used by taxpayers in the year generated and the remainder would be used over the subsequent nine years.

To arrive at the offsetting tax effect of deduction that would otherwise be allowed under current law, it is estimated that qualified taxpayers would be able to deduct approximately $270 million in qualified taxes in the 2026 taxable year. Applying an average tax rate of 7 percent results in an offsetting revenue gain of approximately $20 million, resulting in a net revenue loss of approximately $120 million in the 2026 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

Senate Floor Analysis, dated May 27, 2025.

Support

Bay Area Council; California Chamber of Commerce; California Forever, Inc.; California Manufacturers and Technology Association; California Taxpayers Association; Contra Costa Building and Construction Trades Council; East Bay Leadership Council; Fresno Business Council; Industrial Environmental Association; Inland Empire Economic Partnership; Innovation Tri-Valley Leadership Group; Los Angeles Area Chamber of Commerce; North Bay Leadership Council; San Joaquin Valley Manufacturing Alliance; San Jose Chamber of Commerce; Silicon Valley Leadership Group; and Western Wood Preservers Institute.

Opposition

None received.

ARGUMENTS

None on file.

LEGISLATIVE CONTACT

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