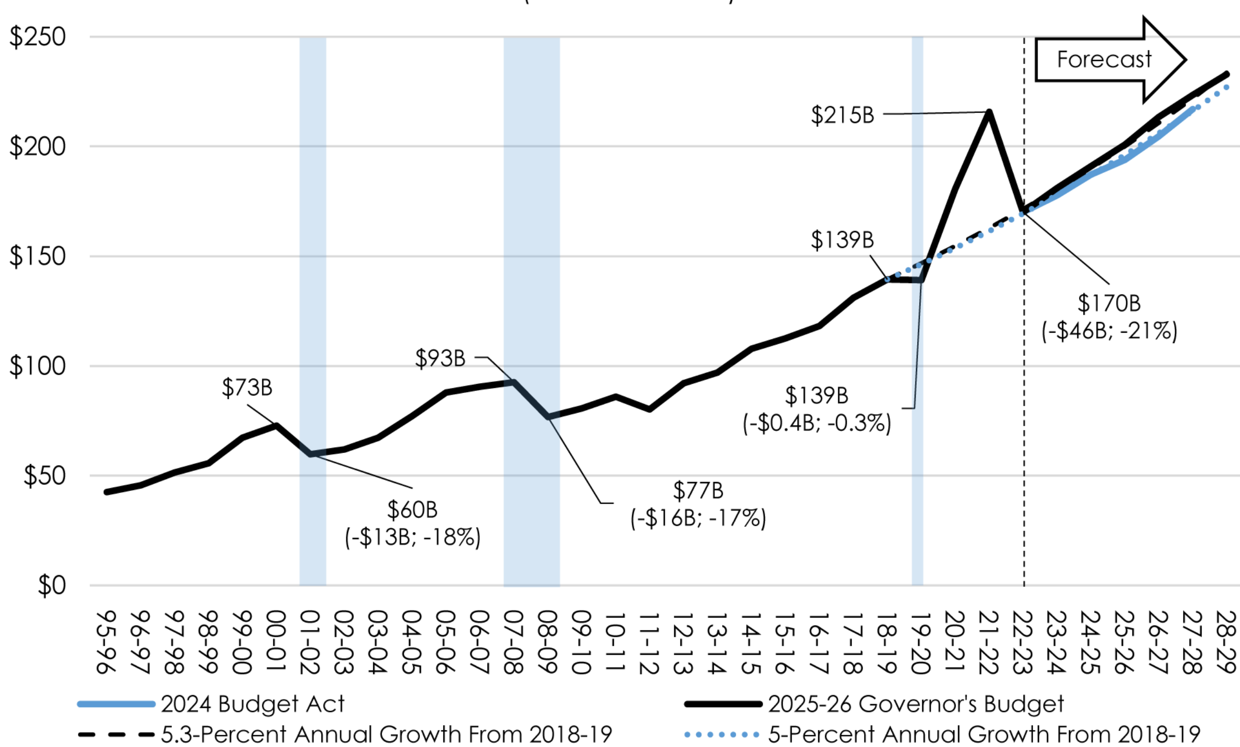
REVENUE ESTIMATES

The economy has generally performed better than expected at the 2024 Budget Act, which led to a meaningful upgrade to the economic forecast in the near-term and to modest upward revisions in the long-term. In particular, the economic forecast's personal income growth projection for California in 2024 is nearly 50 percent higher than projected in the Budget Act, due in part to higher actual and projected wage growth tied to technology sectors. Additionally, the stock market rose substantially in 2024, with the S&P 500 outperforming the Budget Act forecast by 13 percent in the third quarter of 2024. Finally, through November when the Governor's Budget forecast was finalized, General Fund cash receipts exceeded the Budget Act forecast by $7.5 billion, driven by overages in receipts from personal income tax ($4.8 billion), corporation tax ($2 billion), not otherwise classified revenues ($854 million), pooled money interest ($251 million), and insurance ($199 million), offset by a shortfall of $708 million in sales tax that was due to November receipts shifting into December.

The stronger-than-anticipated performance of the economy, stock market, and cash receipts, combined with an improved economic outlook result in an upgrade to the revenue forecast. Before accounting for transfers and tax policy proposals, General Fund revenue is projected to be approximately $16.5 billion, or 2.7 percent, higher than assumed in the 2024 Budget Act over the budget window—from fiscal year 2023-24 through fiscal year 2025-26. The three main drivers of the upgrade were personal income tax ($12.6 billion), corporation tax ($2.5 billion) and pooled money interest ($2.0 billion). The stronger stock market and higher economic wage growth tied to technology sectors disproportionately affect high-income earners, leading to upgrades to the personal income tax forecast, notably through higher capital gains realizations and withholding receipts. The corporate income tax was revised higher due mainly to lower projected usage of credits and net operating losses (NOLs) by corporations and, to a lesser extent, higher corporate profits. Projected interest revenue earned on the Pooled Money Investment Account is revised higher due largely to a higher projected account balance.

Overall, the broader long-term picture of state revenues remains largely unchanged and is modestly upgraded from the 2024 Budget Act. Following a two-year surge of 55 percent through 2021-22 and a correction of 21 percent in 2022-23, revenues from the Big Three—personal income tax, corporation tax, and sales tax—have stabilized and are projected to grow 6.4 percent in 2023-24, followed by normal rates of growth averaging a little over 5 percent through the end of the forecast. As shown in the Big Three Revenues Long-Term Trajectory figure, the projected revenue levels through 2028-29 are consistent with an average annual growth of 5.3 percent from pre-pandemic levels in 2018-19, slightly higher than the projected annual growth of 5 percent at Budget Act. These figures exclude the impact of Budget Act and Governor's Budget policies, including the credit limitation and NOL suspension.

Big Three Revenues Long-Term Trajectory
(Dollars in Billions)



Projected revenue figures exclude the impact of Budget Act tax policies and proposed Governor's Budget policies.
Shaded bars indicate previous U.S. recessions.

These revenue projections assume continued but moderating economic growth along with a stock market that, while projected to be roughly flat through 2025 and 2026, is significantly higher than the levels assumed in the 2024 Budget Act. If financial markets perform significantly worse or better than assumed, the revenue picture will likely change accordingly. Several risks remain, including stock market volatility, an economic recession, or any shocks that would disproportionately impact high-income earners.

BUDGET WINDOW

The Budget General Fund Revenue Forecast figure compares the revenue forecasts, by source, in the 2024 Budget Act and the 2025-26 Governor's Budget. Excluding tax policy proposals, General Fund revenues in the Budget are projected to be $16.5 billion higher over the budget window. After accounting for the revenue impact of tax policy proposals, General Fund revenues are projected to be $16.6 billion higher. The upgrades relative to the 2024 Budget Act forecast are driven primarily by the personal income tax, and to a lesser extent the corporation tax and the Pooled Money Investment Account interest forecasts.

- **Revenues from the Big Three**—The Big Three revenue sources, before accounting for policy proposals, are projected to be higher by $15.3 billion over the budget window due to a $12.6 billion upward revision to the personal income tax forecast, a $2.5 billion upward revision to the corporation tax forecast, and a $174 million upward revision to the sales tax forecast.
- **Minor Revenues**—Insurance, alcoholic beverage, cigarette taxes, and interest revenue from the Pooled Money Investment Account are higher by $2.3 billion over the budget window, due primarily to a $2 billion upgrade in the pooled money interest forecast as higher balances remaining in the account are projected to generate higher interest for longer periods. Projected revenue from insurance tax is higher by $283 million due to stronger growth in insurance premiums.
- **Other Minor Not Otherwise Classified Revenues**—Unclassified revenues are $1.2 billion lower over the budget window due to shifts in the timing of federal payments related to wildfires and COVID-19 Pandemic costs, with $1.3 billion in these cost recoveries shifting outside of the budget window from 2024-25 to 2026-27.
- **Tax Policy Proposals**—Tax policy proposals are projected to increase General Fund revenues by $186 million in 2025-26.

2025-26 Governor's Budget
General Fund Revenue Forecast
Reconciliation with the 2024 Budget Act
(Dollars in Millions)

Source	2024 Budget Act	Governor's Budget	Change From Budget Act Forecast	
Budget Window				
Personal Income Tax	$355,661	$368,302	$12,641	3.6%
Corporation Tax	112,397	114,895	2,497	2.2%
Sales & Use Tax	102,403	102,577	174	0.2%
Insurance Tax	12,088	12,371	283	2.3%
Alcoholic Beverage	1,267	1,270	2	0.2%
Pooled Money Interest	5,930	7,978	2,047	34.5%
Cigarette	124	112	-12	-9.8%
Otherwise Not Classified Revenues	12,618	11,439	-1,179	-9.3%
Revenues Excluding Proposals	$602,488	$618,942	$16,454	2.7%
Tax Policy Proposals	0	186	186	n/a
Revenues	$602,488	$619,128	$16,640	2.7%

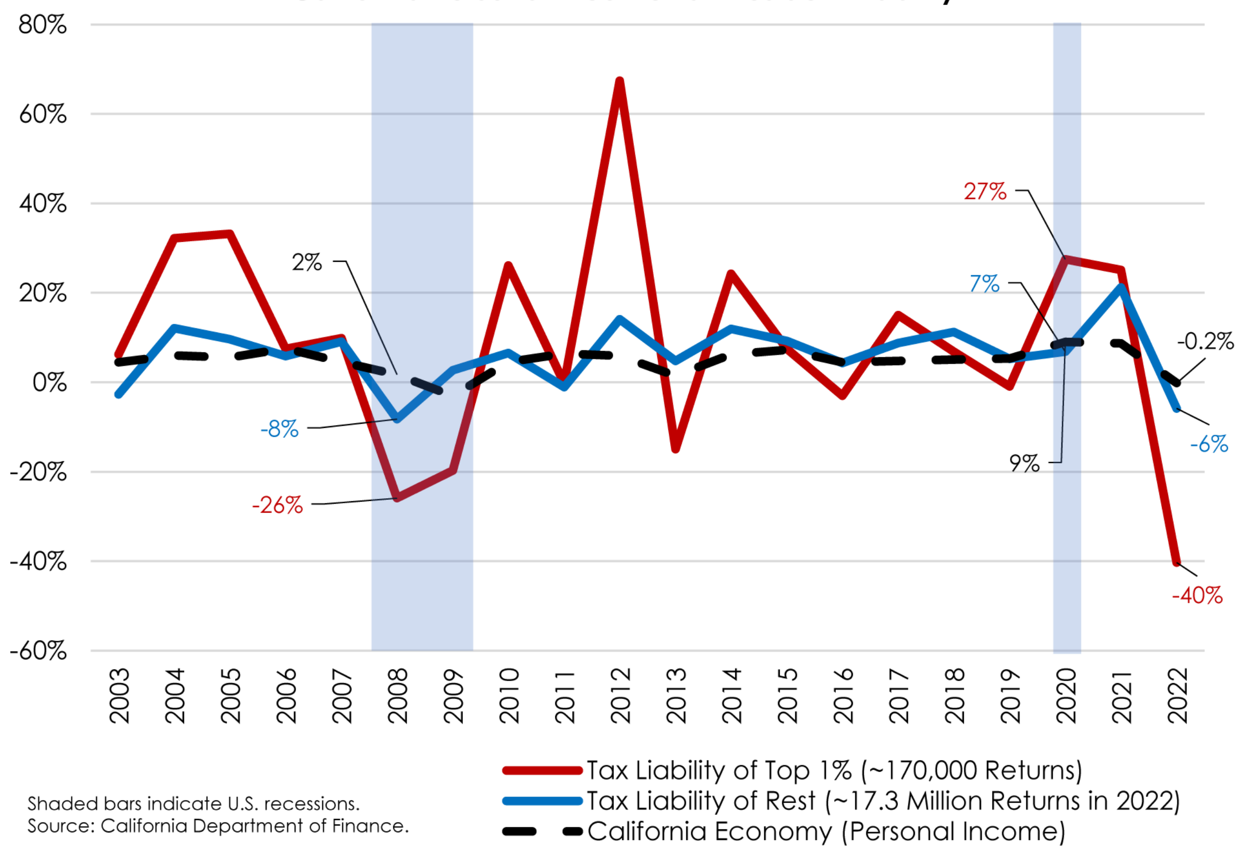
PERSONAL INCOME TAX

The personal income tax is the state's largest revenue source. Excluding pass-through entity elective tax credits, the personal income tax is estimated to account for over 67 percent of General Fund revenues before transfers in 2023-24.

Within the personal income tax, in the 10 years through 2022, wages comprised approximately 59 percent of tax liability on average for all tax returns, and the share of capital gains was approximately 16 percent. In tax year 2022, the most recent year for which complete tax return data is available, wages represented 66 percent of tax liability while capital gains comprised 13 percent. This was a significant decrease from the capital gains' share of 25 percent in 2021 when capital gains realizations hit an all-time high as a share of the economy due to federal stimulus and a surging stock market. Given that wages also include stock-based compensation, a significant share of personal income tax depends on financial markets and individuals' decisions on when to buy and sell stocks.

The highest-income Californians pay the largest share of the state's personal income tax. In 17 of 20 years through 2021, the top one percent of income earners share of total resident personal income tax liability has been greater than 40 percent. For the 2022 tax year, the top one percent of income earners, or over 170,000 tax returns, paid nearly 39 percent of personal income taxes, down from 50 percent in 2021. This was due mainly to a substantial decline in capital gains realizations in 2022 as a result of a weaker stock market and lessening impact from federal stimulus during the pandemic. High-income taxpayers' tax liability tends to be volatile as they earn a larger share of their total income from capital gains and stock-based compensation. To illustrate, capital gains realizations increased by $146 billion, or 72.1 percent, from 2020 to 2021 before decreasing from $349 billion in 2021 to $156 billion in 2022, a decline of 55 percent. Similarly, withholding increased by 20.2 percent in 2021 but declined by 1.2 percent in 2022 due in part to volatility in stock-based compensation. As illustrated in the California Personal Income Tax Resident Liability Growth figure, the top one percent's tax liability is highly volatile and often unconnected to the growth of the broader economy. For example, the tax liability of the top one percent decreased by 40 percent in 2022 while the California economy remained fairly flat.

California Personal Income Tax Resident Liability



Shaded bars indicate U.S. recessions.
Source: California Department of Finance.

These two related phenomena—significant reliance of the General Fund on capital gains and stock-based compensation, and on taxes paid by a small portion of the population—underscore the difficulty of forecasting personal income tax revenue. Proposition 2 helps address some of the state's revenue volatility by requiring the transfer of a portion of capital gains revenue greater than 8 percent of General Fund tax revenue to the Rainy Day Fund and to pay down state debts.

Before accounting for tax policy proposals, the personal income tax forecast is $12.6 billion, or 3.6 percent, higher through the budget window compared to the 2024 Budget Act forecast, due to upward revisions of $2.2 billion in 2023-24, $4.6 billion in 2024-25, and $5.9 billion in 2025-26. Higher actual cash receipts, capital gains, withholding, and a stronger economic forecast all positively contributed to the significant upgrade.

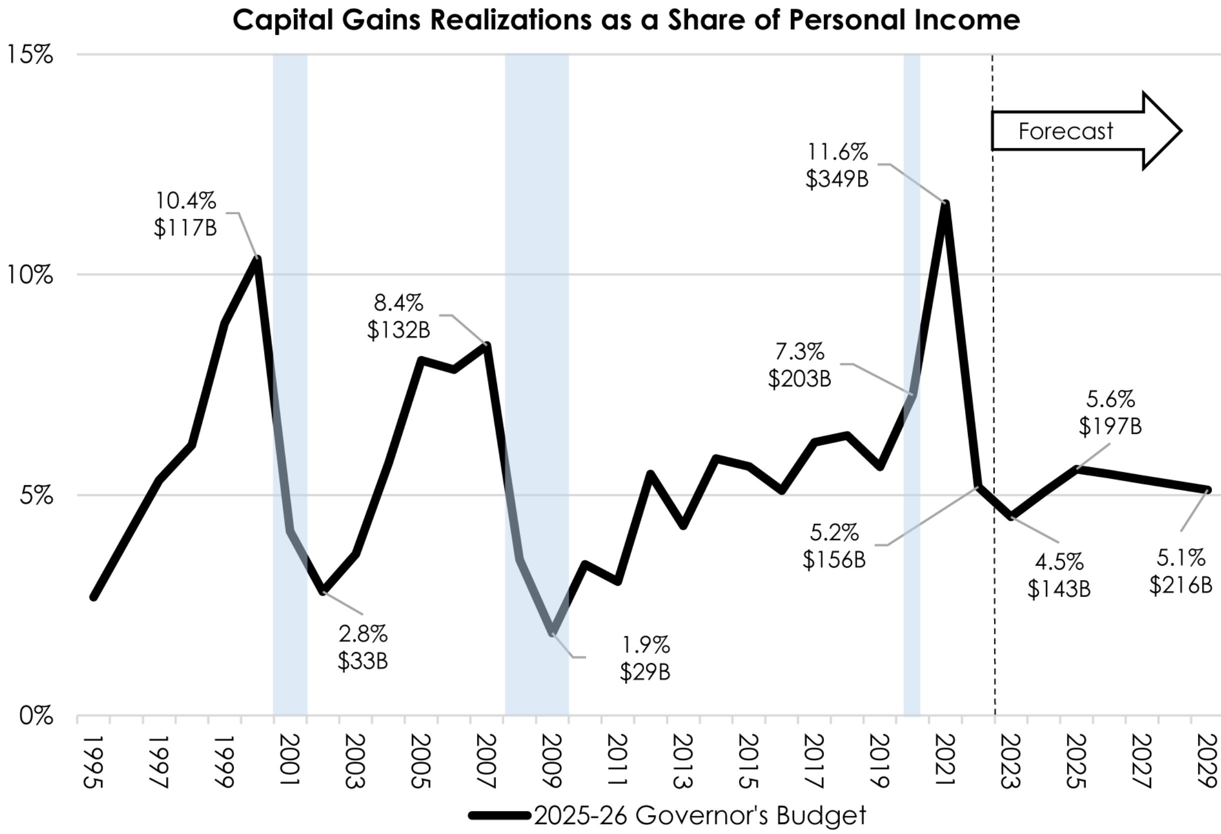
Personal income tax receipts were $4.8 billion above the 2024 Budget Act forecast through November. This was due primarily to higher estimated payments, which were $2.1 billion above forecast. In addition, refunds were lower by $1.5 billion, withholding receipts were $800 million higher, and other payments on net were $400 million above forecast.

CAPITAL GAINS

Capital gains realizations were revised higher relative to the 2024 Budget Act forecast and contribute over $6 billion to the overall personal income tax forecast upgrade. This upward revision is supported by growth in the stock market and stronger-than-expected cash results related to tax years 2023 and 2024.

The 2024 Budget Act forecast projected $137 billion in capital gains realizations in 2023—a 12-percent year-over-year decline from 2022, which followed the 55-percent year-over-year decline from record-high realizations reported in 2021. Cash data related to tax year 2023 indicates the decline in capital gains realizations in tax year 2023 was smaller than previously projected, currently estimated at around 8.5 percent. Additionally, the stock market has risen significantly in 2024 and the S&P 500 is projected to average nearly 5,900 in the first quarter of 2025, compared to 4,900 projected for that quarter in the Budget Act, or a 20-percent upgrade. Due to higher estimated payments of $2.1 billion through November, the Governor's Budget projects capital gains realizations to increase 20 percent in 2024 and 15 percent in 2025, higher than the 15-percent and 10-percent growth rates assumed in the Budget Act.

Capital gains realizations as a share of personal income reached a record-high of 11.6 percent in 2021, exceeding the 2007 pre-Great Recession peak of 8.4 percent and more than a full percentage point higher than the previous record of 10.4 percent in 2000. Following these peaks in 2007 and in 2000, capital gains as a percent of personal income declined to 1.9 percent in 2009 and to 2.8 percent in 2002, which represented peak-to-trough declines in capital gains realizations of 78 percent and 72 percent, respectively. As shown in the Capital Gains as a Percentage of Personal Income figure, following its record share in 2021, capital gains realizations reverted to 5.2 percent of personal income in 2022 and are assumed to decline to 4.5 percent of personal income in 2023. This represents a peak-to-trough decline in capital gains realizations of 59 percent from 2021 to 2023. The Governor's Budget forecast projects capital gains realizations to reach 5.6 percent of personal income in 2025 before gradually moderating to 5 percent of personal income by 2030.



Shaded bars indicate previous U.S. recessions.
Source: California Department of Finance, 2025-26 Governor's Budget Forecast.

The Capital Gains Proposition 2 Revenue figure shows Proposition 2 revenues from capital gains as a percentage of total General Fund tax revenue. The amount of capital gains revenue in the General Fund can vary greatly over time and from year to year. For instance, capital gains contributed $14.4 billion to the General Fund in 2019, increased significantly to $36 billion in 2021—its highest amount ever—and are estimated to decrease back to $14 billion in 2023.

Capital Gains Proposition 2 Revenue
As a Percent of General Fund Tax Revenues
(Dollars in Billions)

Calendar Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023[e/]	2024[e/]	2025[e/]	2026[e/]
Capital Gains Realizations	$55	$52	$100	$80	$115	$120	$113	$144	$154	$145	$203	$349	$156	$143	$171	$197	$202
Prop 2 Revenue from Capital Gains	$4.7	$4.2	$10.4	$7.6	$11.3	$11.8	$11.5	$14.1	$15.4	$14.4	$20.6	$36.0	$15.4	$14.0	$17.0	$19.6	$20.1
Fiscal Year	**09-10**	**10-11**	**11-12**	**12-13**	**13-14**	**14-15**	**15-16**	**16-17**	**17-18**	**18-19**	**19-20**	**20-21**	**21-22**	**22-23**	**23-24[e/]**	**24-25[e/]**	**25-26[e/]**
Prop 2 Revenues from Capital Gains	$3.0	$4.5	$6.0	$9.6	$8.7	$11.4	$11.7	$12.3	$14.5	$15.1	$16.3	$25.2	$29.8	$15.0	$14.9	$17.7	$19.7
Total General Fund Revenues[1/]	$87	$92	$85	$98	$103	$114	$119	$122	$135	$144	$145	$187	$224	$179	$192	$209	$218
Capital Gains Percentage	3.4%	4.9%	7.1%	9.8%	8.5%	10.1%	9.9%	10.0%	10.7%	10.4%	11.2%	13.5%	13.3%	8.4%	7.7%	8.5%	9.1%

[e/]Estimated
[1/]Excluding transfers
Source: California Department of Finance, 2025-26 Governor's Budget Forecast.

WITHHOLDING

Higher withholding contributed $3.3 billion to the overall personal income tax upgrade. Withholding was revised higher in 2024 due to strong cash results since April. Withholding is projected to grow 8 percent in 2024, higher than the 6.5-percent growth expected in the 2024 Budget Act. Higher withholding growth in 2024 has been driven in part by recent strength from technology-related sectors—information, manufacturing, and professional and technical services. In 2023, withholding from technology-related sectors grew 1.9 percent, in line with overall withholding growth. However, in the first 11 months of 2024, withholding from technology-related sectors increased 11.5 percent year-over-year compared to a growth of 4.9 percent for all other sectors.

OTHER PERSONAL INCOME COMPONENTS

Other personal income components comprised the remainder of the upgrade to the personal income tax forecast. Most notably, the higher economic forecast for California personal income led to higher taxable partnership, business, and pension income. In addition, nonresident and fiduciary income were revised higher, due primarily to higher capital gains realizations.

MENTAL HEALTH SERVICES FUND

Modeled closely after federal income tax law, California's personal income tax is imposed on net taxable income—gross income less exclusions and deductions. The tax rate structure is progressive over the income spectrum. Since the 2012 tax year, the marginal tax rates range from 1 percent to 12.3 percent, not including a 1-percent surcharge on taxable income above $1 million for the Mental Health Services Act tax imposed by Proposition 63 beginning in 2004. Proposition 30 created three additional income tax brackets beginning in 2012 with rates of 10.3 percent for taxable income above $500,000, 11.3 percent for taxable income above $600,000, and 12.3 percent for taxable income above $1 million, with the income thresholds indexed for inflation. Proposition 30 held these tax brackets in effect for seven years—from tax years 2012 to 2018. Voters approved Proposition 55 in November 2016, extending the three additional tax brackets through tax year 2030.

Revenue from the 1-percent surcharge imposed by Proposition 63 is transferred to the Mental Health Services Fund and used to fund mental health programs. The Budget projects annual revenues of $2.8 billion in 2023-24, $3.2 billion in 2024-25, and $3.6 billion in 2025-26 for this fund. Over the budget window, these transfers to the Mental Health Services Fund are higher by nearly $900 million compared to the 2024 Budget Act. The upward revision generally reflects the higher forecast for capital gains realizations in the 2025-26 Governor's Budget, which are disproportionately earned by higher-income taxpayers. The General Fund and the Mental Health Services Fund shares of personal income tax revenues for 2023-24 through 2025-26 are shown in the Personal Income Tax Revenue figure.

Personal Income Tax Revenue

(Dollars in Millions)

	2023-24 Preliminary	2024-25 Forecast	2025-26 Forecast
General Fund	$113,380	$121,106	$133,685
Mental Health Services Fund	$2,784	$3,231	$3,586
Total	**$116,164**	**$124,338**	**$137,271**

Source: California Department of Finance, 2025-26 Governor's Budget Forecast.

CORPORATION TAX

Before accounting for tax policy proposals, the corporation tax forecast is higher by $2.5 billion, or 2.2 percent, in the budget window from 2023-24 to 2025-26. Corporation tax cash receipts exceeded the 2024 Budget Act forecast by $2 billion through November despite higher refunds of nearly $800 million. The cash overage was primarily due to estimated payments that were higher by $1.6 billion.

The primary driver of higher corporation tax revenues, contributing about $2.4 billion, is lower expected use of business tax credits and NOL deductions, due mainly to higher anticipated revenue from the 2024 Budget Act policy to temporarily limit the use of business tax credits and suspend the use of NOLs for large businesses. The policy impact was revised higher due to the assumption that a lower percentage of existing tax credits will be used while the credit limitation is in effect. This updated assumption is supported by recent cash results, particularly higher estimated payments related to tax year 2024.

Due to higher payments related to tax year 2023, corporate taxable profits were upgraded by about $900 million in the budget window. Meanwhile, audit payments and fees paid by limited liability companies were upgraded by about $400 million due to higher cash receipts. Partially offsetting those positive factors are higher levels of refunds related to prior tax years stemming from audits, court resolutions, and settlements. This is projected to lower revenues by $1.2 billion in the budget window. This amount includes over $600 million in unanticipated refunds related to prior tax years that were issued through early December.

SALES AND USE TAX

Sales tax revenue is expected to account for approximately 16 percent of General Fund revenues excluding transfers and loans in 2025-26, down from nearly 19 percent in 2022-23 and much lower than its historic share of nearly 40 percent four decades ago in 1983-84. Sales tax has steadily declined in relevance to the state budget as tangible goods—on which sales tax revenues rely almost exclusively due to California’s narrow sales tax base—have accounted for a shrinking proportion of overall economic spending. California’s sales tax base includes largely the same products it did in the mid-twentieth century when services spending, which is almost entirely untaxed in California, accounted for a much smaller proportion of economic spending.

During the pandemic, this trend briefly reversed as tangible goods spending benefited from pandemic-era distortions including significant inflation in large taxable goods categories such as automobiles and furniture and a substitution of goods for services in consumer’s overall spending. During that time, taxable sales increased as a percentage of personal income from approximately 27 percent in 2018-19 to nearly 29 percent in 2021-22 and sales tax revenues increased by 26.3 percent over that same period. As these distortions have unwound over the past few years, California taxable sales have declined even as the economy has recovered and continued to grow. California sales tax revenues increased by just 1 percent from 2021-22 to 2023-24 whereas the California economy, as proxied by personal income, increased by 8.8 percent over that same period.

Before accounting for tax policy proposals, the sales tax forecast is less than 1 percent, or just under $200 million, higher in the budget window relative to the 2024 Budget Act forecast. After correcting for $600 million in shifting from November to December, cash receipts through November are within 0.5 percent of the Budget Act forecast. The small upward revision in the sales tax forecast was due to a slight upgrade in the economic outlook that has pushed taxable sales growth rates in 2024-25 and 2025-26 about a tenth of a percentage point higher.

Consistent with the 2024 Budget Act, the normalization process following the pandemic disruptions noted above is assumed to be mostly complete by the fourth quarter of 2024. Taxable sales growth is projected to resume at a rate of roughly 3 percent annually in 2024-25 and 2025-26, consistent with the typical relationship between consumer spending, personal income, and taxable sales. Nevertheless, the projected average annual growth in sales tax of 4.2 percent from 2018-19 to 2028-29 compares unfavorably with projected growth of 5.3 percent for the Big Three revenues during the same period. Despite the completion of the acute effects of normalization, sales tax revenue is expected to continue to grow more slowly than the budget and economy overall due to the long-term divergence between California's sales tax base and consumption spending overall.

RISKS AND UNCERTAINTY

The Budget revenue forecast is based on an assumption of continued but slowing economic growth. Additionally, outside of the impact of tax policies proposed in the Budget, revenue projections are based on current state and federal laws. Continued stock market strength and improved economic growth support the forecast assumptions of resumption to normal revenue growth following the post-pandemic revenue correction. However, several risk factors could negatively impact the economy and state revenues going forward. For instance, stock market and asset price volatility and declines, shocks that disproportionately impact high-income earners, and geopolitical turmoil are all issues posing risk to ongoing economic and revenue growth.

New risks have also arisen from uncertainty about federal policy. As noted in the Economic Outlook and Demographic Information Chapters, several of the policies contemplated by the incoming federal administration are likely to negatively impact the national and state economies through inflationary impacts and extreme immigration measures. If the economic outlook is dampened by these policies, state revenues will also subsequently decline.

Additionally, revenue forecasting is always subject to significant uncertainty, even if the underlying economy and the stock market are performing in line with expectations. This is particularly acute in the personal income and corporate income tax forecasts, as liability for those taxes also depends on taxpayer behavior and timing of when assets are sold, when credits and NOLs are used by corporations, and corporate refunds related to prior tax years. Recent developments that increase this uncertainty include the 2024 Budget Act policy to limit business tax credits and suspend NOLs for larger businesses and an increase in corporate refunds related to prior years that were issued or are projected to be issued in 2024-25. In addition, with many provisions in the Tax Cuts and Jobs Act expiring at the end of 2025, anticipation of potential federal tax policy changes could affect the timing of capital gains realizations and other income. As a result, revenues could still end up more than $20 billion higher or lower within the budget window—even if the economy and asset markets perform largely in line with expectations. The principal drivers that could lead to higher or lower revenues include higher or lower personal income tax withholding receipts, capital gains realizations, corporate taxable profits, the use of corporate net operating losses and business incentive tax credits, and corporate refunds.

TAX PROPOSALS

The Budget includes several tax proposals as described below. These proposals combined are estimated to increase General Fund revenues by a total of $186 million in 2025-26.

CALIFORNIA FILM AND TELEVISION TAX CREDIT EXPANSION

The state established the California Film and Television Tax Credit in 2009 to encourage film and television producers to locate shooting and spending on wages and other expenditures in-state. The program has been over-subscribed since its inception and has awarded over $3 billion in tax credits across three rounds of the program. The fourth round of the California Film and Television Tax Credit program (Program 4.0) was established by the 2023 Budget Act at $330 million in tax credits per year from fiscal year 2025-26 to 2029-30. Program 4.0 included new provisions to improve and support the California film industry, including workforce investments, diversity requirements, and a refundability provision in order to benefit a wider range of productions and to ensure the competitive program will maximize economic benefits to the state.

The Budget proposes to increase the total annual California Film and Television Tax Credit 4.0 award cap from $330 million to $750 million for the fiscal years 2025-26 through 2029-30. This proposal is expected to reduce revenues by $15 million in 2025-26. Costs are projected to increase in subsequent years, reaching $209 million by the end of the multiyear period in 2028-29, and peaking outside of the multiyear period. While this expansion applies to fiscal years beginning in 2025-26, credits are claimed four years after allocation on average because film productions typically take multiple years and credits are only claimed once a verified tax return is filed.

MILITARY RETIREMENT INCOME EXCLUSION

California is home to 141,000 military retirees as of 2023. Current California and federal law fully tax military retirement pay and survivor benefits as income. Beginning in tax year 2025, the Budget proposes to exclude from income for state tax purposes: (1) retirement pay received by a taxpayer from the federal government for service in the uniformed services; and (2) annuity payments received by a qualified taxpayer pursuant to a Department of Defense Survivor Benefit Plan. The exemption would apply for up to $20,000 of military retirement income. Additionally, the exemption would be limited to taxpayers with up to $250,000 in income if filing jointly and up to $125,000 in income for single filers. The proposal is estimated to reduce revenues by $130 million in 2025-26 and by $85 million annually thereafter.

SINGLE SALES FACTOR FOR FINANCIAL INSTITUTIONS

Multi-state and multi-national corporations pay taxes in California by computing how much of their taxable income is allocated to California. To calculate this amount, corporations use an apportionment factor that represents the share of business activity they conduct in the state. Most companies are required to use the single sales factor formula, which is based on the location of a company’s sales. However, financial institutions, companies in extraction industries, and agricultural producers are required to use the three-factor apportionment formula, which also accounts for the location of the company’s properties and payroll in the calculation.

Beginning in tax year 2025, the Budget proposes to move financial institutions to single sales factor apportionment, aligning financial institutions with nearly all other corporations, and rewarding businesses for locating in the state. By increasing the weight of the sales factor, single sales factor apportionment is generally more beneficial than three-factor apportionment to firms with a larger physical presence in the state as they can exclude their property and payroll factors from the calculation. This proposal is estimated to increase revenues by $330 million in 2025-26 and by more than $250 million annually thereafter.

WILDFIRE SETTLEMENTS INCOME EXCLUSION

Under current federal and state law, certain settlements related to wildfire disasters can be subject to taxation. As a result, California has previously provided income exemptions on a case-by-case basis following certain large wildfires to ensure all types of settlements related to those specific wildfire disasters are exempt from state taxation. Wildfire disasters are expected to continue to occur in California. To provide relief to taxpayers, the Budget proposes to exempt all wildfire settlements from state taxation for settlements paid in tax years 2025 through 2029, regardless of when the fire occurred.

EXTENSION OF PASS-THROUGH ENTITY ELECTIVE TAX

Under current federal law as enacted in the Tax Cuts and Jobs Act of 2017, personal income taxpayers are limited to deducting no more than $10,000 of state and local tax (SALT) payments on their federal return while business entities are able to fully deduct state and local income taxes. The 2021 Budget Act enacted a new pass-through entity elective tax (PTET) allowing taxpayers who have income from pass-through entities to electively pay a tax at the business entity level and receive a state personal income tax credit for the same amount. The PTET does not negatively impact state revenues and is estimated to have saved California taxpayers billions of dollars per year on their federal taxes by allowing them to more fully deduct their state and local taxes.

The PTET is scheduled to sunset after 2025 along with the federal SALT cap. To provide certainty that the PTET will continue to be available to California taxpayers if a SALT cap remains in effect, the Budget proposes to extend the PTET, subject to the federal SALT cap being extended.