

REVENUE ESTIMATES

Before accounting for transfers and tax policy proposals, the General Fund revenue forecast for 2024-25 through 2026-27—the budget window—is upgraded by \$16.8 billion, or 2.5 percent, relative to the Governor's Budget forecast. This is due mainly to the personal income tax, which, excluding the impact of the Pass-Through Entity Elective Tax (PTET), accounts for \$15.7 billion of the upgrade, driven largely by a spike in 2025 capital gains realizations that provided a significant boost to 2025-26 revenues. In addition, corporation tax, excluding the impact of the PTET, is down by \$1.6 billion, sales tax is up by \$244 million, and the PTET itself contributes \$2.1 billion to the upgrade. Overall, the May Revision revenue upgrade reflects higher cash results, with General Fund cash receipts being \$11.9 billion higher through April, combined with a modestly upgraded stock market outlook and a relatively unchanged economic forecast.

As a result of strong non-withholding personal income tax payments through April, which exceeded the Governor's Budget forecast by \$6.4 billion, the May Revision forecast estimates capital gains realizations increased to \$287 billion in 2025—\$64 billion higher than projected in the Governor's Budget and the second-highest level of capital gains realizations ever, following the peak of \$349 billion reached in 2021. The 2025 level of capital gains realizations represents 8 percent of total personal income, an elevated share of the economy seen only during three periods in the past 30 years: the Dot Com Boom, the real estate bubble in the mid-2000s, and the COVID-19 Pandemic surge. Unlike after those prior periods when financial markets declined at least 20 percent from their highs and capital gains dropped substantially, the May Revision forecast assumes a moderation in stock market growth rather than a significant stock market correction.

This results in capital gains realizations declining below 2025 levels but remaining above Governor's Budget projections through the end of the multi-year period—2027-28 through 2029-30.

The economy has generally remained resilient in the face of multiple shocks, including the Iran war, frequently shifting tariff policy, and more restrictive immigration policy, all of which have increased uncertainty, raised costs, or constrained labor supply. As a result, while the economic forecast reflects some near-term weakness due to the Iran war, it continues to project modest economic growth largely in line with the Governor's Budget forecast, and its overall impact on the revenue forecast throughout the entire budget window is roughly neutral.

The significant \$16.8 billion upgrade relative to the Governor's Budget, when excluding transfers, is almost entirely tied to higher stock market prices, which drive revenue gains through the personal income tax with higher capital gains revenue (contributes \$13.5 billion to the \$15.7 billion upgrade in personal income tax) and higher stock-based compensation (contributes \$2.2 billion). Revenues are upgraded every year through the end of the multi-year window in 2029-30; however, because recent revenue strength is tied to significant stock market gains that are assumed to moderate moving forward, a substantial portion of the upgrade in 2025-26 does not persist in 2026-27 and subsequent years.

BUDGET WINDOW

Before accounting for tax policy proposals, General Fund revenues, excluding transfers and loans, are projected to be \$16.8 billion higher than assumed in the Governor's Budget over the budget window. While there are various changes as summarized in the May Revision General Fund Revenue Forecast Reconciliation with the Governor's Budget figure, this upgrade is driven largely by the personal income tax, and, to a lesser extent, the corporation tax due to higher-than-expected PTET payments. Including tax policy proposals but excluding transfers, General Fund revenues are upgraded by \$18.1 billion in the budget window. After accounting for tax policy proposals and transfers, General Fund revenues are upgraded by \$7.1 billion.

- **Revenues from the Big Three**—Before accounting for tax policy proposals, the Big Three revenues—personal income, corporation, and sales taxes—are projected to be higher by \$16.5 billion, due largely to strong cash results related to tax year 2025 that reflect a significant increase in capital gains realizations under the personal income tax. The forecast for personal income tax is revised up by \$13.6 billion,

corporation tax revenues are higher by \$2.7 billion, and the sales tax forecast is upgraded by \$244 million.

- **PTET**—Higher PTET payments related to tax year 2025 contribute a net revenue gain of \$2.1 billion to the Big Three revenue upgrade, due to credit use against the personal income tax lagging payments under the corporation tax. The net gain reflects higher corporation tax revenue of \$4.3 billion and lower personal income tax revenue of \$2.2 billion due to the PTET.
- **Minor Revenues**—Insurance taxes, alcoholic beverage taxes, cigarette taxes, and interest earned on pooled money, are higher by \$227 million in the budget window due mainly to an upgrade of \$256 million in the insurance tax forecast.
- **Other Minor Not Otherwise Classified Revenues**—Unclassified revenues are \$138 million higher in the budget window.
- **Transfers and Loans**—Excluding transfers to the Budget Stabilization Account (BSA) and transfers to the Projected Surplus Temporary Holding Account, transfers and loans are projected to increase General Fund revenues by \$10.2 billion, a \$570 million downgrade relative to what was assumed in the Governor's Budget.
 - The May Revision includes a new \$9.7 billion transfer from the General Fund to the Projected Surplus Temporary Holding Account in 2026-27.
- **BSA Transfers**—BSA transfers are projected to increase General Fund revenues by \$8.1 billion in the budget window, a downgrade of \$725 million relative to the Governor's Budget due primarily to a larger deposit in 2026-27. The May Revision maintains the \$7.1 billion withdrawal from the BSA in 2025-26, which was assumed in the Governor's Budget.
- **Tax Policy Proposals**—Tax policy proposals are projected to increase General Fund revenues by \$1.3 billion relative to the Governor's Budget.

2026-27 May Revision
General Fund Revenue Forecast
Reconciliation with the 2026-27 Governor's Budget
(Dollars in Millions)

Source	Governor's Budget	May Revision	Change From Governor's Budget Forecast	
Fiscal 2024-25				
Personal Income Tax	\$130,178	\$131,328	\$1,150	0.9%
Corporation Tax	41,338	41,757	419	1.0%
Sales & Use Tax	33,602	33,596	-6	0.0%
Insurance Tax	4,298	4,298	0	0.0%
Alcoholic Beverage	414	414	0	0.0%
Pooled Money Interest	3,081	3,081	0	0.0%
Cigarette	37	37	0	0.0%
Other Revenue	5,557	5,538	-19	-0.3%
Subtotal	\$218,506	\$220,049	\$1,543	0.7%
Transfer To/From BSA	4,767	4,598	-169	-3.5%
Other Transfers	9,036	8,992	-44	-0.5%
Total	\$232,309	\$233,639	\$1,330	0.6%
Fiscal 2025-26				
Personal Income Tax	\$137,840	\$146,847	\$9,007	6.5%
Corporation Tax	41,702	43,287	1,585	3.8%
Sales & Use Tax	34,401	34,588	188	0.5%
Insurance Tax	4,370	4,510	141	3.2%
Alcoholic Beverage	417	413	-4	-0.9%
Pooled Money Interest	3,018	2,801	-217	-7.2%
Cigarette	35	35	0.4	1.0%
Other Revenue	3,924	4,024	100	2.5%
Subtotal	\$225,706	\$236,506	\$10,800	4.8%
Transfer To/From BSA	7,100	7,100	0	0.0%
Other Transfers	2,356	1,836	-521	-22.1%
Total	\$235,162	\$245,442	\$10,279	4.4%
Fiscal 2026-27				
Personal Income Tax	\$142,202	\$145,610	\$3,408	2.4%
Corporation Tax	43,528	44,192	664	1.5%
Sales & Use Tax	35,085	35,148	63	0.2%
Insurance Tax	4,612	4,728	115	2.5%
Alcoholic Beverage	419	415	-4	-0.9%
Pooled Money Interest	2,165	2,360	195	9.0%
Cigarette	34	34	0.1	0.4%
Other Revenue	2,992	3,049	57	1.9%
Tax Policy Proposal	10	1,304	1,294	12943.5%
Subtotal	\$231,047	\$236,839	\$5,793	2.5%
Transfer To/From BSA	-3,023	-3,579	-556	18.4%
Other Transfers	-638	-10,386	-9,747	1526.8%
Total	\$227,385	\$222,875	-\$4,511	-2.0%
Three-Year Total Excluding Transfers			\$18,136	
Three-Year Total including Transfers			\$7,099	

PERSONAL INCOME TAX

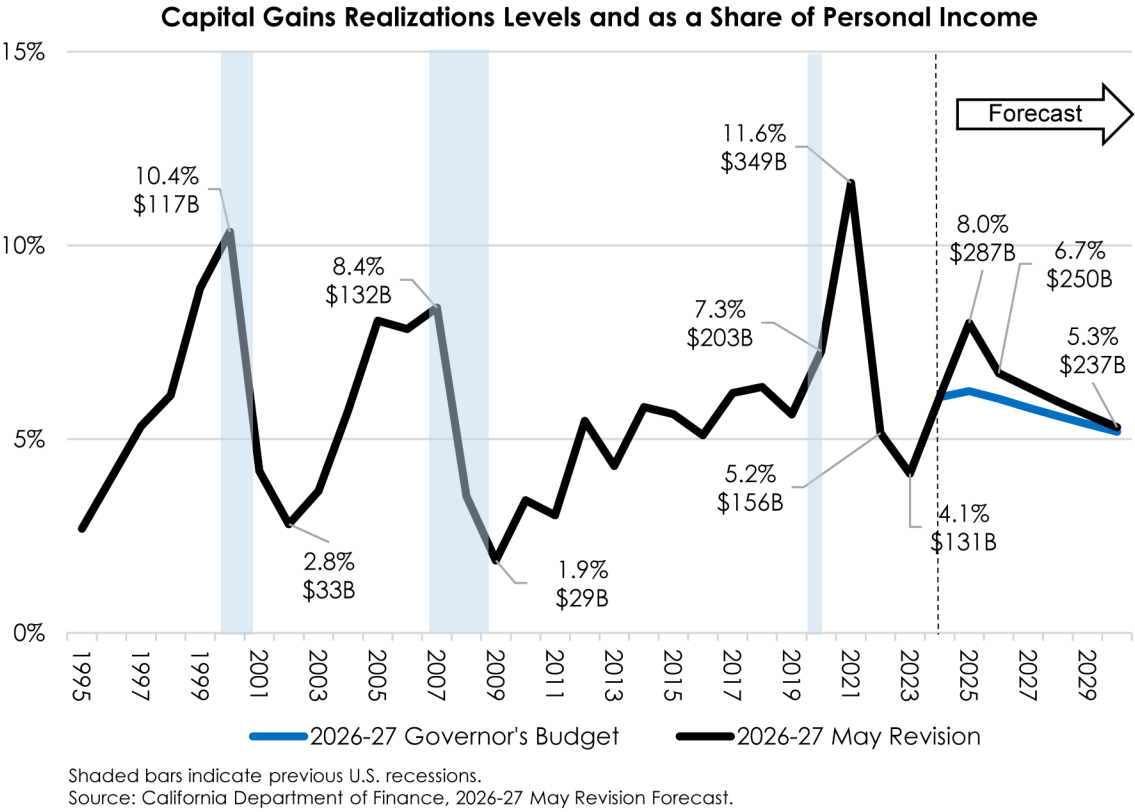
Before accounting for tax policy proposals, the personal income tax forecast is higher by \$1.1 billion in 2024-25 and \$9 billion in 2025-26, reflecting strong cash results through April 2026 that are largely related to tax year 2025 and indicate that capital gains realizations for tax year 2025 were significantly above the Governor's Budget forecast. The personal income tax forecast is higher by \$3.4 billion in 2026-27, a smaller upgrade compared to 2025-26 as capital gains realizations are projected to decline 13 percent in 2026 from unsustainably high levels in 2025.

The upgraded PTET forecast results in higher credit use under the personal income tax, negatively impacting the personal income tax forecast by \$2.2 billion in the budget window. Therefore, when excluding PTET, the personal income tax is upgraded by \$15.7 billion over the budget window, which comprises nearly all the total \$16.8 billion upgrade for all taxes.

Capital gains and capital gains-related income, including nonresident and fiduciary income, explain approximately \$13.5 billion of the upgrade, while withholding contributes an additional \$2.2 billion. Changes to other income items, such as business income, pension income, and dividend income, largely offset each other.

Personal income tax cash receipts were approximately \$8.1 billion over the Governor's Budget forecast through April, due primarily to a \$6.4 billion overage in non-withholding payments that are mostly related to tax year 2025. In addition, personal income tax withholding receipts exceeded the Governor's Budget forecast by \$1.5 billion, with roughly \$400 million of this gain due to earlier collection of receipts projected for May. Personal income tax refunds were \$299 million lower than projected in the Governor's Budget forecast.

Informed by cash results through late April, capital gains realizations are projected to increase from \$223 billion in 2024 to \$287 billion in 2025—a \$64 billion upgrade compared to the Governor's Budget's projection. This is a projected 39-percent year-over-year increase in 2025 and follows a 58-percent year-over-year increase in 2024. Therefore, 2025 capital gains are projected to reach more than double the \$131 billion level of capital gains in 2023. In 2025, capital gains realizations' share of personal income is estimated to increase to 8 percent, as illustrated in the Capital Gains Realizations Levels and Share of Personal Income figure.



Reflecting continued gains in equity markets since the Governor's Budget, the S&P 500 forecast is upgraded from 6,625 to 7,013, or by 5.9 percent, in the second quarter of 2026. As a result, capital gains realizations' share of personal income is projected at 6.7 percent in 2026, upgraded from the 6-percent share projected in the Governor's Budget. However, given the unsustainably high level of capital gains estimated for 2025, that upgraded share still results in a projected year-over-year decline of approximately 13 percent. Still, capital gains realizations are upgraded from \$225 billion to \$250 billion in 2026 and from \$227 billion to \$247 billion in 2027. Capital gains realizations are then assumed to decline slightly from 2028 on and reach 5 percent of personal income by 2031. Overall, relative to the Governor's Budget forecast, capital gains levels are upgraded throughout the multi-year forecast.

Withholding growth decelerated slightly from 9.5 percent in 2024 to 8.1 percent in 2025. The strength in withholding is largely attributable to equity markets' growth in 2024 and 2025, which resulted in higher levels of stock-based compensation for employees of large California-based technology companies. Withholding growth is projected to moderate to 5.3 percent in 2026 but is still upgraded from the 4-percent growth

projected in the Governor's Budget, due mainly to higher equity prices boosting stock-based compensation.

CORPORATION TAX

Before accounting for tax policy proposals, the corporation tax forecast is higher by \$2.7 billion in the budget window due to an upgrade to the Pass-Through Entity Elective Tax (PTET) forecast. The PTET forecast accounts for \$4.3 billion of the corporation tax forecast upgrade and is partially offset by lower personal income tax revenue due to higher PTET credit use.

Corporation tax cash receipts exceeded the Governor's Budget forecast by nearly \$2.8 billion through April, due entirely to higher PTET payments. Excluding PTET payments, corporation tax receipts were \$53 million below the Governor's Budget forecast, with lower estimated payments of \$732 million and lower miscellaneous payments of \$120 million, mostly offset by lower refunds of \$799 million.

Excluding the PTET, corporation tax revenues are downgraded by \$1.6 billion, due primarily to a lower forecast for corporate taxable profits (contributes -\$2.2 billion), consistent with actual tax data from 2024, which reflect a year-over-year decline of 2 percent, and lower non-PTET receipts. Additionally, revenues are projected to be lower from prior-year settlements (contributes -\$200 million). Partially offsetting the weakness in taxable profits and prior-year settlements, cash receipts from limited liability company (LLC) fees and taxes have been robust, suggesting strong business formation and leading to an upgrade for collections in 2025-26 and 2026-27 (contributes \$800 million).

SALES AND USE TAX

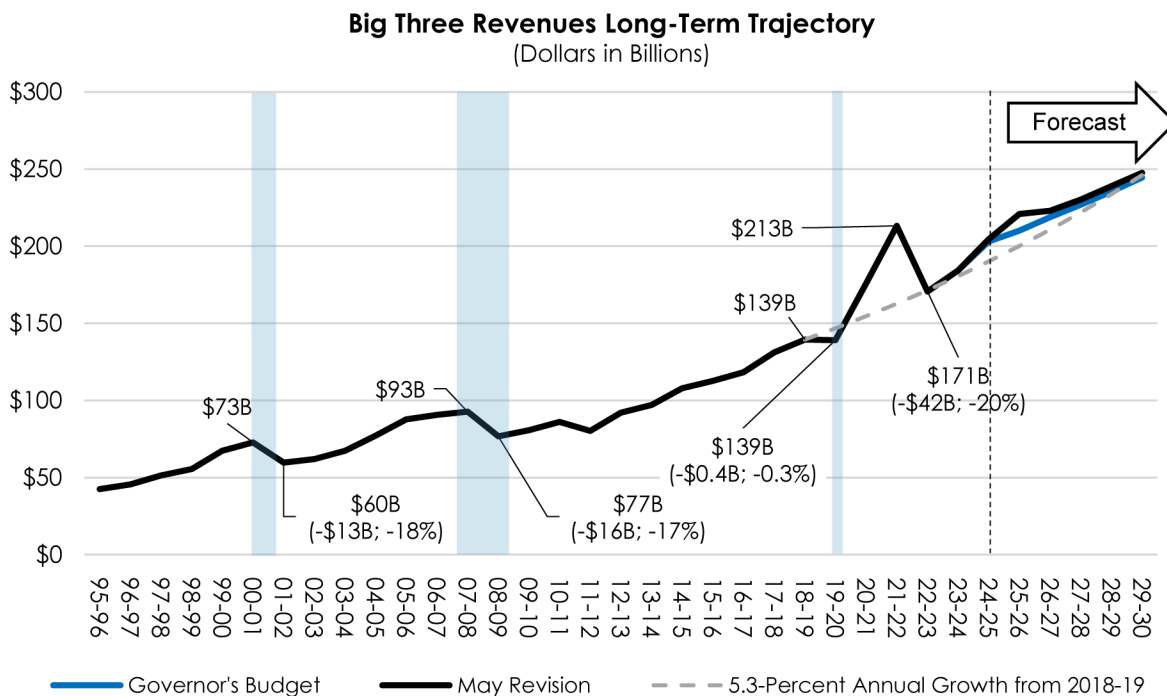
Before accounting for tax policy proposals, the sales tax forecast is \$6 million lower in 2024-25, \$188 million higher in 2025-26, and \$63 million higher in 2026-27.

Sales tax cash receipts were \$82 million, or 0.3 percent, above the Governor's Budget forecast through April 2026 as investment activity in capital equipment has been modestly above forecast and was upgraded throughout the budget window. There are offsetting inflationary impacts affecting the sales tax: higher fuel prices due to the Iran war raise inflation while the lower effective tariff rate results in lower inflation than previously assumed. Overall, consumer spending is largely unchanged from the Governor's Budget forecast, as fuel prices are projected to moderate and therefore not

crowd out taxable consumption. However, higher diesel fuel prices increase diesel sales tax transfers from the General Fund to the Public Transportation Account in 2026-27, contributing to slower sales tax growth and the narrowing revenue upgrade in net sales tax revenues in 2026-27.

LONG-TERM FORECAST

As shown in the Big Three Revenues Long-Term Trajectory figure, revenues are projected to remain above their long-term trend of 5.3-percent annual growth from pre-pandemic levels throughout the multi-year. Revenue upgrades peak in 2025-26 and narrow beginning in 2026-27 as stock market growth is projected to moderate and capital gains realizations are assumed to decline to a more normal share of the economy. However, General Fund revenues related to the Big Three revenue sources are cumulatively higher by \$9.9 billion from fiscal years 2027-28 through 2029-30. Despite the upgrade in revenues, expectations for long-term economic growth are largely unchanged. California personal income growth is unchanged from the Governor's Budget projection in 2026, lower by 0.3 percentage point in 2027, and within 0.1 percentage point of the Governor's Budget forecast on average between 2028 and 2030.



Projected revenue figures exclude the impact of the business credit limitation and suspension of net operating loss deductions and proposed May Revision tax policies. Shaded bars indicate previous U.S. recessions.

The Long-Term Revenue Forecast table below summarizes the projections for each of the Big Three from 2024-25 through 2029-30. Big Three revenue growth surged 12.4 percent in 2024-25, driven by strong personal income tax and corporation tax revenues, as a result of strong stock market gains and the temporary business credit limitation and net operating loss deduction suspension. The robust projected Big Three revenue growth of 8.7 percent in 2025-26 is driven by personal income tax revenues, which benefit from the surge in capital gains realizations in 2025. In 2026-27, growth is just 0.7 percent due to a modest decline in personal income tax revenues as capital gains in 2026 are projected to decline year-over-year from unsustainably high levels. Modest but below-average growth continues throughout the multi-year as personal income tax revenues are negatively impacted by slightly declining capital gains realizations and corporation tax revenues are negatively impacted by higher credit use following the expiration of the temporary credit limitation and net operating loss suspension at the end of 2026. Sales tax revenue growth is relatively stable beginning in 2025-26 but continues to grow at a much slower rate than the overall economy due to its narrow base consisting mainly of tangible goods.

Long-Term Revenue Forecast—Three Largest Sources

(General Fund Revenue—Dollars in Billions)

	2024-25	2025-26 ^{e/}	2026-27 ^{e/}	2027-28 ^{e/}	2028-29 ^{e/}	2029-30 ^{e/}
Personal Income Tax	\$131.3	\$146.8	\$145.6	\$150.3	\$155.9	\$161.5
(Year-over-Year Change)	14.0%	11.8%	-0.8%	3.2%	3.7%	3.6%
Corporation Tax	\$41.8	\$43.3	\$45.0	\$44.4	\$45.3	\$47.0
(Year-over-Year Change)	17.8%	3.7%	4.0%	-1.4%	2.0%	3.8%
Sales and Use Tax	\$33.6	\$34.6	\$35.6	\$37.0	\$38.1	\$39.2
(Year-over-Year Change)	0.8%	3.0%	3.0%	3.9%	3.0%	2.9%
Total	\$206.7	\$224.7	\$226.3	\$231.7	\$239.3	\$247.7
(Year-over-Year Change)	12.4%	8.7%	0.7%	2.4%	3.3%	3.5%

^{e/}Estimated

Source: California Department of Finance, 2026-27 May Revision Forecast.

RISKS AND UNCERTAINTY

Economic recession risks remain elevated due to unpredictable federal policy, geopolitical risks due to the Iran war that will continue to negatively impact consumers across the country if higher global oil and gas prices persist, and a softer job market. While the economy has remained resilient thus far, some of that strength is driven by higher stock prices and investment in artificial intelligence, which is more susceptible to a reversal due to a change in sentiment, rather than underlying strength of the consumer, which would be more durable. The May Revision assumes ongoing

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moderate economic growth as near-term inflationary impacts from the Iran war are projected to ease. However, if higher fuel prices and inflation persist, then recessionary risks increase as higher fuel prices would crowd out consumption.

California's revenue is impacted significantly by the stock market due to the state's progressive personal income tax structure and reliance on high-income earners. Stocks have risen substantially over the past three years, with the S&P 500 increasing 78 percent from the beginning of 2023 to the end of 2025, with the gains driven in large part by large technology companies benefiting from the artificial intelligence boom. Given the stock market's very large gains as well as the concentration of those gains in companies benefitting from the outsized investment in artificial intelligence, the stock market could be vulnerable to a significant downturn. If a significant market downturn were sustained, it would negatively impact state revenue through multiple channels, including reduced capital gains income, business income, nonresident income, fiduciary income, and stock-based compensation. If a market downturn of more than 20 percent—comparable to the decline in 2022—were to occur in 2026 and be sustained through the end of the year, revenue could be \$15 billion to \$20 billion below forecast within the budget window, even if there were no economic recession. If coupled with an economic recession, revenue would be even lower.

Even in the absence of a stock market correction, revenue forecasts are subject to greater uncertainty, both to the upside and the downside, when stock market prices drive a larger share of revenue. One upside risk is the potential revenue impact of large Initial Public Offerings (IPOs) that may occur with regard to SpaceX, Anthropic, and OpenAI, each of which has a large workforce in California. The May Revision does not make any explicit adjustments for the potential impact of these IPOs given the uncertainty as to their timing, actual IPO valuation, and whether the employees at these companies have stock-based compensation that will become taxable at the IPO. The IPOs themselves are also uncertain, as they can be pulled back if market conditions worsen or if the companies feel that they are not getting the valuation they deserve. In recent years, more private companies have allowed employees to sell their stock prior to an IPO, which means there is less of a backlog of stock-based compensation that would become taxable at the IPO. Once companies make public their financial documents at the Securities and Exchange Commission prior to the IPO, then estimates of potential one-time revenue gains from a backlog of stock-based compensation, if it exists, can be made and incorporated into the forecast.

TAX POLICY PROPOSALS

The May Revision includes the following new tax policy proposals:

- **Permanent Credit Limitation**—Effective beginning in tax year 2027 when the current temporary credit limitation and net operating loss suspension is lifted, the May Revision proposes a more modest permanent business tax credit limitation that protects small businesses while ensuring that larger corporations pay a minimum level of tax. The new proposed limit is the greater of \$5 million per company per year or 50 percent of a company's tax liability. The \$5 million threshold provides protection for smaller businesses while the 50-percent tax liability threshold allows larger firms to use a significant portion of their tax credits over the \$5 million threshold. Unlike the current temporary credit limitation and net operating loss suspension that is in effect from 2024 through 2026, net operating losses can be fully utilized and are not impacted. This proposal helps with restoring the state's structural balance and is projected to increase revenues by \$850 million in 2026-27, \$1.7 billion in 2027-28, and similar ongoing revenue gains in subsequent years.
- **Digital Prewritten Software Tax**—Effective January 1, 2027, the May Revision proposes to apply the sales tax to sales of digital prewritten software, regardless of how the product is delivered to the purchaser, whether on a disc or physical medium, electronic transmission and local hosting (download), or remote access through the internet, including Software-as-a-Service (SaaS), where the customer accesses the software hosted by the vendor but never takes possession of it. Of the 45 states with a statewide sales tax, 35 states tax digital prewritten software delivered electronically and 24 states tax SaaS. This proposal helps with restoring the state's structural balance and is projected to increase General Fund revenues by \$450 million in 2026-27 and \$900 million in 2027-28 and annually thereafter, and it additionally increases local sales tax revenues by \$560 million in 2026-27 and \$1.1 billion in 2027-28 and annually thereafter.
- **Reduce the \$800 Annual Tax for New Businesses by Half**—To encourage the formation of new small businesses, which are a major engine of economic growth in California, the May Revision proposes to reduce the \$800 annual tax paid by limited liability companies, limited partnerships, and limited liability partnerships in their first year to \$400 during the 2027, 2028, and 2029 tax years. This proposal will benefit approximately 250,000 new businesses each year and is expected to provide \$100 million in tax relief per year.

- **Conform to Federal Tax Treatment of Trump Accounts**—Consistent with the state's general practice of conforming to federal law for tax-advantaged savings and retirement accounts, effective beginning in tax year 2026, the May Revision proposes to conform to federal tax treatment of Trump Accounts. This proposal is projected to decrease General Fund revenues by \$1 million in 2026-27, increasing to \$3 million by 2029-30.