



# This Week in State Tax (TWIST)

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## California: Budget Revision Released

Governor Newsom of California recently released his May budget revisions. Importantly, the revised budget contemplates clarifying the law to address the recent Office of Tax Appeals (OTA) decision in *Microsoft*. Recall, in *Microsoft*, the OTA concluded that the full amount of qualifying dividends deducted from income under R&TC section 24411 were includable in the taxpayer's sales factor. As revised, the budget legislation would "clarify" existing law to provide that when a corporation receives income excluded from taxable business income, that income must likewise be excluded from the corporation's apportionment factor. There is no specific effective date associated with this change in the Governor's revised budget. The budget revisions also propose suspending NOL carryover deductions for businesses with California income over \$1 million and limiting business credit usage to \$5 million for tax years 2025, 2026, and 2027. The credit limitation does not apply to the Low-Income Housing and Pass-through Entity Elective tax credits. This is consistent with actions the legislature took for the 2020 and 2021 tax years in light of the COVID-induced budget deficit. The budget notes that if sufficient revenues are determined to be available, the limitations will be reconsidered, as they were for the 2022 tax year when the legislature reinstated the use of NOLs and suspended the limitation on the use of credits. Both the NOL and credit carryover periods would be extended by three years during the period of suspension/limitation. Before the May revisions, Governor Newsom had proposed conforming to the federal 80 percent limitation on the use of NOLs. Please stay tuned for future updates as California's budget negotiations continue.

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