



Golden State Global: How H.R. 1's Tax Overhaul Impacts California-Based Multinationals

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The recently enacted 2025 Tax Act brings significant changes to the U.S. tax code, especially for multinational companies. The international tax landscape is being reshaped, creating both challenges and opportunities for California-based businesses. From Silicon Valley tech firms to Hollywood studios, California's globally focused industries must quickly adapt to these changes. With most provisions taking effect in 2026, the clock is ticking for businesses to reassess their global tax strategies.

Overview

- **Effective date:** Most international provisions apply to tax years beginning after Dec. 31, 2025.
- **U.S. Rate:** The top U.S. rate remains at 21% but the foreign-income rules are overhauled.
- **Action Required:** California-based tech, life science, media and cleantech companies have 18 months to restructure and adjust data pipelines.

The Legislative Foundation

The international changes are embedded in Public Law 119-21. Here are key sections to review with your board, auditors and advisors.

Theme	Key H.R. 1 Sections	What Changed?
• NCTI replaces GILTI	§70323	Renames GILTI to Net CFC Tested Income (NCTI) and repeals the 10% QBAI carve-out.
• 40% NCTI deduction	§70321(a)(2)	Permanent 40% deduction, resulting in 12.6% headline U.S. rate before credits.
• FDDEI replaces FDII	§70321(a)(1)	New 33.34% deduction; asset-based formula removed.
• Foreign-tax-credit tweaks	§70311-§70313	90% credit haircut; 50% foreign-source rule for U.S. inventory sold via foreign branches.
• BEAT survives—10.5%	§70331	Rate rises to 10.5%; credit offsets preserved.
• Interest cap double-hit	§70341	EBITDA base; applies before capitalization rules.
• Downward-attribution fix	§70354	Restores pre-2017 ownership rules.

Why California-Headquartered Groups Should Pay Attention

- **Venture-Backed Growth Models at Risk**
Silicon Valley's SaaS firms, which had moved IP offshore for QBAI protection, now face immediate inclusions. Capital-light structures remain favorable, but only if foreign effective rates exceed ~14% after the 90% credit haircut.
- **Supply-Chain Flexibility for Hardware & Cleantech**
The new 50% foreign-source rule for U.S.-produced inventory (§70313) can reduce residual U.S. tax on goods assembled in Fresno and shipped through L.A./Long Beach.
- **Hollywood & Streaming Royalties Under the Microscope**
Intercompany licensing fees remain a primary trigger for BEAT at the higher 10.5% rate; studios should update service-fee benchmarks before 2026 closings.
- **Renewable-Energy Tax Equity Unchanged for Now**
Title VII of the bill reserved separate clean-energy sections, which do not disturb §45/§48 credits. This gives Bay Area financiers the flexibility to model tax-equity stacks alongside the new interest-cap provisions.

Core Rule Changes: A Deeper Dive

1. Net CFC Tested Income (NCTI)

- **What's Gone:** The 10% deemed return on tangible assets (QBAI).
- **What's New:** A permanent 40% deduction (§70321) plus a 90% credit for foreign taxes.

Example: A Mexican CFC earns \$100 and pays \$5 in tax. U.S. inclusion: \$60; gross U.S. tax = \$12.6; credit = \$4.5; residual = \$8.1 (13.1% combined).

California Impact: Groups with maquiladora operations lose their QBAI shield and will need to revisit advance-pricing and maquila safe-harbor rates.

2. Foreign-Derived Deduction-Eligible Income (FDDEI)

- **Simplified:** Only proof of foreign customer required; asset-based calculation scrapped.
- **Deduction:** 33.34% (§70321).

Tip: Track customer location at order-entry in systems like NetSuite/SAP for seamless export to §250 workpapers.

3. Base Erosion and Anti-Abuse Tax (BEAT) 2.0

- **Threshold Unchanged:** Base-eroding payments exceeding 3% of deductions trigger the tax.

- **Rate:** 10.5% from 2026 forward (§70331).
- **R&D and business credits still offset**

Action for Bay-Area biotech: Assess BEAT liability after 2025 when California-qualified research credits are renewed.

4. Interest Deduction Compression

- **EBITDA base remains** but NCTI and Subpart F income are excluded, lowering the denominator.
- **Pre-capitalization Test:** Limitation applies before §263A, per §70341.

California Impact: Debt-funded acquisitions of L.A. media libraries may now breach the cap in year 1.

5. Ownership & Timing Clean-Up

- **Downward Attribution Repealed (§70354):** Foreign-parent stock is no longer pushed down, preventing surprise CFC status for U.S. subsidiaries.
- **Timing Rule:** Inclusion is required if stock is held at any point during the year, closing the "year-end drop-out" loophole.

Action Plan (August 2025 – December 2026)

Quarter	What to Do	Why
Q3 2025	Build NCTI/FDDEI engine in your tax-data warehouse.	Model scenarios before the budgeting season.
Q4 2025	Renegotiate intercompany royalties & service fees.	Mitigate BEAT at 10.5%.
Q1 2026	Re-draft transfer-pricing reports; embed §250 customer codes.	Substantiate FDDEI claims.
Q2 2026	Refinance external and intercompany debt.	Optimize under new §163(j) and BEAT rules.
Q3 2026	Map ERP expense fields to Form 1118 buckets.	Track direct vs. indirect expenses for new FT limitations.
Q4 2026	Board dry-run on OECD Pillar Two interplay (2027 start).	Check if 14% residual tax rate beats the 15% global minimum.

California-Specific Considerations

- **Research-Heavy Profile:** California businesses account for 28% of U.S. R&D credits. Preserving these credits against BEAT remains crucial.
- **Strategic Gateway:** The West Coast time zone and trade routes enhance the value of the 50% foreign-source inventory rule for exporters.
- **Talent & IP Density:** Tighter CFC inclusions make IP location and workforce mobility a bigger audit target, particularly for cross-border "work-from-anywhere" teams.

Final Thoughts

The 2025 Tax Act presents both opportunities and challenges. While it lowers residual U.S. tax on foreign profits to around 14%, California-based multinationals must overhaul their structures, data systems, and financing within the next 18 months. Treat this window as an opportunity to strategically reset your global tax approach for the next decade.



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