



ARIZONA STATE SENATE
Fifty-Seventh Legislature, Second Regular Session

VETOED
FACT SHEET FOR S.B. 1106/H.B. 2153

internal revenue code; conformity; deductions

Purpose

Retroactive to January 1, 2025, conforms Arizona tax statutes to the U.S. Internal Revenue Code (U.S. IRC) as of January 1, 2026, to reflect changes adopted by the U.S. Congress during 2025. Establishes individual income tax subtractions, modifies individual income tax deductions and increases the Dependent Tax Credit. Declares the state's election to participate in the federal tax credit for individuals who make qualified contributions to school granting organizations (SGOs) and outlines SGO certification and administration requirements.

Background

The Arizona Legislature periodically updates the statutory definition of the U.S. IRC to include any federal provisions that became effective in the preceding calendar year as a means of paralleling the computation of Arizona income tax and other statutory references throughout the Arizona Revised Statutes to the amended U.S. IRC. Tax conformity with the U.S. IRC is deemed necessary because the calculation of Arizona corporate income tax liability begins with federal taxable income. Similarly, federal adjusted gross income (FAGI) is the starting point for individual income tax assessment.

On July 4, 2025, major federal tax changes were enacted through H.R. 1, commonly referred to as the One Big Beautiful Bill. Due to tax code conformity, these federal changes have the potential to impact state revenues. H.R. 1 includes changes that impact federal taxable income and FAGI which the state could conform to by updating the statutory definition of the U.S. IRC (standard conformity). However, H.R. 1 also includes provisions that are not automatically incorporated when updating the definition of U.S. IRC.

According to the Arizona Department of Revenue (ADOR), the estimated impact to the state General Fund associated with standard conformity would be a reduction of \$369.88 million in FY 2026, \$144.57 million in FY 2027 and \$154.28 million in FY 2028. The Joint Legislative Budget Committee fiscal note estimates that S.B. 1106 would reduce state General Fund revenues by \$441.3 million in FY 2026, \$337.2 million in FY 2027, \$363.1 million in FY 2028 and \$296.6 million in FY 2029 ([JLBC Fiscal Note](#)).

Provisions

Conformity

1. Updates the statutory definition of *Internal Revenue Code* to include all provisions in effect as of January 1, 2026, with the specific adoption of all retroactive effective dates, excluding any changes to the U.S. IRC enacted after January 1, 2026.

Individual Income Tax Subtractions

2. Establishes the following individual income tax subtractions, for taxable years beginning January 1, 2025, to the extent not already excluded from Arizona gross income under the U.S. IRC:
 - a) the amount of qualified tips received during the taxable year that is deducted under the federal income tax deduction for qualified tips;
 - b) the amount of qualified overtime compensation received during the taxable year that is deducted under the federal income tax deduction for qualified overtime compensation;
 - c) the amount of a distribution from a Trump Account established pursuant to federal law; and
 - d) the amount of child and dependent care expenses for a *qualifying individual* paid or incurred by the taxpayer for the taxable year that exceeds the amount of the federal Credit for Child and Dependent Care Expenses that the taxpayer received.
3. Establishes the following individual income tax subtractions for taxable years beginning January 1, 2025, capped at an aggregate amount of \$6,000 for a taxpayer who is single, married filing separately or a head of household or \$12,000 for a married couple filing jointly:
 - a) for taxpayers who are at least 60 years old during the taxable year, an amount of up to \$6,000 that is distributed from a pension or retirement account, to the extent not already excluded from Arizona gross income or the U.S. IRC; and
 - b) an amount of up to \$6,000 that is contributed to a Roth individual retirement account during the taxable year, to the extent that the contributions were not deducted in computing FAGI.
4. Requires the individual income tax subtraction for individuals who are at least 60 years old to be reduced by 6 percent of the amount that the taxpayer's income exceeds the subtraction, if:
 - a) the taxpayer's Arizona gross income is \$75,000 or more and the taxpayer is single, married filing separately or a head of household; or
 - b) the taxpayer's Arizona gross income is \$150,000 or more for a married couple filing jointly.

Individual Income Tax Deductions

5. Replaces the Arizona-specific standard deduction by coupling with the federal standard deduction, including the annual inflation adjustment.
6. Allows, for taxable years beginning January 1, 2026, a taxpayer that takes the standard deduction to increase the deduction by an amount equal to the total amount of the taxpayer's charitable contributions, rather than up to 25 percent of qualifying contributions, and caps the contributions at:

- a) \$1,000 for a single person or married person filing separately; and
 - b) \$2,000 for a married couple filing jointly.
7. Allows a taxpayer to deduct up to \$10,000 of state and local taxes in lieu of the full amount of the federal itemized deduction for state and local taxes allowed under the U.S. IRC.

Dependent Tax Credit

8. Increases the Dependent Tax Credit from \$100 to \$125 for each dependent who is under 17 years old at the end of the taxable year.

SGOs

9. Declares that Arizona elects to participate in the federal tax credit for individuals who make qualified contributions to SGOs.
10. Requires ADOR to comply with all federal laws and regulations to administer the federal SGO credit to ensure Arizona is eligible to participate in taxable years beginning January 1, 2027, and to annually submit all required information to the U.S. Secretary of the Treasury for Participation.
11. Allows a nonprofit organization in Arizona that is exempt, or that has applied for exemption, from federal taxation to apply to ADOR for certification as an SGO and requires ADOR to certify that the SGO meets the federal requirements and applicable regulations or guidance issued by the U.S. Secretary of the Treasury.
12. Requires ADOR, by January 1 of each year, to:
- a) submit to the U.S. Secretary of the Treasury a list of certified SGOs located in Arizona; and
 - b) post the list on ADOR's official website.
13. Requires ADOR to adopt rules and publish and prescribe forms and procedures necessary to administer SGO certification requirements.
14. Allows, beginning January 1, 2027, an ADOR-certified SGO that is on the list submitted to the U.S. Secretary of the Treasury to provide scholarships to eligible students for any qualified elementary or secondary education expenses to the extent allowed under federal law.

Miscellaneous

15. Defines terms.
16. Makes technical and conforming changes.
17. Becomes effective on the general effective date, retroactive to January 1, 2025.

Governor's Veto Message

The Governor indicates in her [veto message](#) that S.B. 1106 gives tax breaks to special interests while raising taxes on working seniors and she states that questions on tax conformity outside of the package introduced by the Governor in [EO 2015-15](#) should be decided through budget negotiations.

Senate Action

FIN 1/14/26 DP 4-3-0
3rd Read 1/15/26 17-12-1

House Action

WM 1/14/26 DP 5-4-0-0
3rd Read 1/15/26 31-27-2
(S.B. 1106 was substituted for H.B. 2153 on 3rd
Read)

Vetoed by the Governor 1/16/26

Prepared by Senate Research
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MG/hk