Franchise Tax Board

SUMMARY ANALYSIS OF AMENDED BILL

Author:	Dutton	Analyst:	Gail Hall	Bill Number:	SB 472
Related Bills:	See Prior Analysis	Telephone:	845-6111	Amended Date:	May 14, 2009
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Exclusion/50 Percent Of Gain From Sale Or Exchange Of Capital Asset Held More Than 3 Years

____ DEPARTMENT AMENDMENTS ACCEPTED. Amendments reflect suggestions of previous analysis of bill as introduced/amended __________________.

_X_ AMENDMENTS IMPACT REVENUE. A new revenue estimate is provided.

____ AMENDMENTS DID NOT RESOLVE THE DEPARTMENTS CONCERNS stated in the previous analysis of bill as introduced/amended __________________.

____ FURTHER AMENDMENTS NECESSARY.

____ DEPARTMENT POSITION CHANGED TO __________________.

_X_ REMAINDER OF PREVIOUS ANALYSIS OF BILL AS INTRODUCED FEBRUARY 26, 2009, STILL APPLIES.

_X_ OTHER – See comments below.

SUMMARY

This bill would allow taxpayers to exclude from gross income 50 percent of net capital gain, as specified.

SUMMARY OF AMENDMENTS

The May 14, 2009, amendments made the following changes to the bill:

- Revised the bill's effective/operative date provisions,
- Resolved implementation consideration No. 1 and argument/policy concern No. 2 discussed in the department's analysis of the bill as introduced February 26, 2009. (See Appendix A)

Except for the "Effective/Operative Date" and "Economic Impact" discussions, the remainder of the department's analysis of the bill as introduced February 26, 2009, still applies. In addition, the unresolved Implementation Consideration and Arguments/Tax Policy Concerns discussed in the department's analysis of the bill as introduced February 26, 2009, have been provided for convenience.

Board Position:			Legislative Director	Date
____ S	____ NA	____ NP		
____ SA	____ O	____ NAR	Brian Putler	01/13/10
____ N	____ OUA	_X_ PENDING		

EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective immediately upon enactment and would be specifically operative for taxable years beginning on or after January 1, 2012, and before January 1, 2015. In addition, the provisions of this bill would only apply to capital assets purchased on or after the effective date and held for more than three years. For example, if the bill were enacted on June 1, 2009, the effective date would be June 1, 2009. The provisions added by this bill would be repealed by their own terms on December 1, 2015.

POSITION

Pending.

IMPLEMENTATION CONSIDERATION

The department has identified the following implementation concern. Department staff is available to work with the author's office to resolve this concern and any other concerns that may be identified.

1. It appears this bill's 50 percent exclusion could be applied in addition to the small business stock or personal residence capital gain exclusions. If this was not the intent of the author, amendments are necessary.

ECONOMIC IMPACT

Revenue Estimate

The revenue impact of this bill is estimated to be as shown in the following table:

Estimated Revenue Impact of SB 472 Effective for taxable years Beginning On Or After January 1, 2012 and Before January 1, 2015. Enacted After June 30, 2009 $ Millions			
2010/11	2011/12	2012/13	2013/14
-$5	-$85	-$440	-$980

This analysis does not consider the possible changes in employment, personal income, or gross state product that could result from this bill.

Revenue Discussion

The revenue impact was estimated using a microsimulation model. This model simulates the tax liability of each individual taxpayer under current and proposed tax laws based on personal and financial data such as filing status, taxable income, capital gains, and tax rates. Included below is an explanation of how the 2012 taxable revenue estimate was calculated. The same process was applied to taxable years 2013 and 2014.

The revenue impact of taxable year 2012 was estimated as follows:

First, data was gathered from a sample of 2007 personal income tax (PIT) returns. Simulation results show that this bill would reduce PIT capital-gain tax from $10.76 billion to $6.77 billion, a revenue loss of -$3.99 billion for the 2007 taxable year. The -$3.99 billion revenue loss was extrapolated to -$2.94 billion for taxable year 2012 based on the Department of Finance's (DOF) forecast of capital gain income.[1] The 2012 estimated revenue loss is smaller than the 2007 revenue loss due to DOF's forecasted drop in capital gain income for taxable years 2008 and 2009. It is estimated that six percent of the -$2.94 billion revenue loss for taxable year 2012 comes from assets purchased on or after the operative date of June 30, 2009. Therefore, the gross impact of this bill for the 2012 taxable year is estimated at approximately -$180 million (-$2.94 billion x 6%).

Second, the -$180 million estimated revenue loss for taxable year 2012 was adjusted downward to account for potential increases of sales of capital assets due to the 50 percent exclusion provision under this bill, and upward to account for the additional impact of this bill on corporations and partnerships. Both these adjustments nearly cancel each other out, resulting a slightly larger net revenue loss of -$181 million.

Finally, the taxable-year estimates are converted to fiscal-year estimates and shown in the above table. For example, the above revenue loss of -$181 million for the 2012 taxable year would occur in three fiscal years; -$75 million in the 2011/12 fiscal year, -$95 million in 2012/13, and -$11 million in 2013/14. The small revenue loss for 2010/11 is due to the estimated delay of sales of capital assets in 2011 to take advantage of lower capital gains tax rates in future years.

ARGUMENTS/POLICY CONCERNS

1. Existing federal and state laws provide for an alternative minimum tax, commonly called AMT, which ensures that taxpayers with substantial economic income and credits, deductions, and other preference items do not completely escape taxation. Legislation creating the federal and state exclusion of gain from the sale or exchange of small business stock includes a tax preference item for a portion of the excluded income. Similar treatment of the exclusion proposed by this bill would maintain fairness in the tax system.

[1] DOF Forecast For Capital Gain Income: -55%, -10%, +25%, and +21% for 2008, 2009, 2010, and 2011, respectively.

2. As introduced, the bill would allow investments in other states to qualify for the 50 percent exclusion. If the author's intent is to encourage investment in California, it is suggested that the bill be amended to provide such a limitation.

LEGISLATIVE STAFF CONTACT

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APPENDIX A
Resolved Implementation Consideration and Argument/Policy Concern
Analysis Of The Bill As Introduced February 26, 2009

Resolved Implementation Consideration Discussed In The Department's Analysis Of The Bill As Introduced February 26, 2009.

1. This bill has no requirement for the netting of capital gains and losses before determining the amount of capital gain exclusion. This conflicts with current federal and state laws relating to capital gains and losses. If the intent of the author was to maintain the current netting rules for capital gains and losses, amendments would be necessary.

Resolved Argument/Policy Concern Discussed In The Department's Analysis Of The Bill As Introduced February 26, 2009

2. This bill would encourage the sale of capital assets purchased prior to January 1, 2009. If this bill is intended to provide an incentive for future investments, the operative date should be revised to apply to the gains from the sale or exchange of capital assets purchased on or after January 1, 2009, with the repeal date extended appropriately.