Franchise Tax Board

ANALYSIS OF AMENDED BILL

Author:	Ashburn, et al.	Analyst:	Angela Raygoza	Bill Number:	SBX3 37
Related Bills:	See Legislative History	Telephone:	845-7814	Amended Date:	October 14, 2009
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Principal Residence Credit

SUMMARY

This bill would expand the availability of the qualified principal residence credit.

SUMMARY OF AMENDMENTS

The October 14, 2009, amendments removed language that would have addressed the Budget Act of 2009 and added language that would do the following:

- Restore authority for the principal residence credit for purchases, as specified;
- Increase the total amount of credit available for allocation reducing the total by 70 percent of the amount allocated to each taxpayer;
- Clarify the certification submission process for the credit, and
- Make an appropriation to fund the department's costs to implement the bill.

This is the department's first analysis of the bill.

PURPOSE OF THE BILL

According to the language of the bill, the purpose is to address the fiscal emergency declared by the Governor by proclamation on December 19, 2008.

EFFECTIVE/OPERATIVE DATE

As an urgency statute, this bill would be effective immediately upon enactment and specifically operative for purchases that occur on or after March 1, 2009, and before July 3, 2009, and for purchases that occur beginning on or after the effective date of this bill and before March 1, 2010.

POSITION

Pending.

Board Position:			Department Director	Date
_______ S	_______ NA	_______ NP		
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_______ N	_______ OUA	___X___ PENDING		

ANALYSIS

FEDERAL LAW

Existing state and federal laws provide various tax credits designed to provide tax relief for taxpayers who incur certain expenses (e.g., child adoption) or to influence behavior, including business practices and decisions (e.g., research credits or economic development area hiring credits). These credits generally are designed to provide incentives for taxpayers to perform various actions or activities that they may not otherwise undertake.

First-Time Homebuyer's Credit

Housing and Economic Recovery Act of 2008 (Public Law 110-289)

A "first-time homebuyers" credit was enacted by the Housing and Economic Recovery Act of 2008. The Act added a new refundable tax credit for "first-time homebuyers." The amount of the credit is the lesser of $7,500 or 10 percent of the home's purchase price. The credit is phased out for taxpayers with adjusted gross income[1] (AGI) between $75,000 and $95,000 ($150,000 and $170,000 for joint filers). The credit applied to principal residences purchased after April 8, 2008, and before July 1, 2009.

The credit is recaptured under the terms of Internal Revenue Code (IRC) section 36(f) over 15 years with no interest charge, beginning with the second tax year after the tax year in which the home is purchased. If the home is sold before the 15-year period ends, the remaining credit must be recaptured in the year of sale.

American Recovery and Reinvestment Act of 2009 (Public Law 111-5)

The "first-time homebuyers" credit was modified by the American Recovery and Reinvestment Act of 2009. In general, for homes purchased after December 1, 2008, and before December 1, 2009, the maximum credit allowed is increased to $8,000 ($4,000 for married individuals filing separately). The credit is no longer required to be recaptured unless the taxpayer sells the qualified residence within 36 months. The credit applies to homes that are financed by exempt mortgage revenue bonds or located in the District of Columbia.

STATE LAW

Newly enacted state law, SBX2 15 (Ashburn, Stats. 2009 Third Extraordinary Session, Ch. 11), provides a tax credit in the amount of 5 percent of the purchase price of a qualified principal residence or $10,000, whichever is less. The credit is allowed for one purchase of a qualified principal residence by an individual and for purchases made on or after March 1, 2009, and before March 1, 2010. Within one week of the sale of the qualified principal residence, the seller is required to provide to the purchaser and to the Franchise Tax Board (FTB) certification that the residence has never been previously occupied.

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[1] Adjusted gross income, as defined by IRC section 62, means gross income, which includes all income from whatever source derived, adjusted for certain allowable amounts, including IRA contributions, alimony paid, moving expenses, and Keogh account contributions.

The tax credit is allocated by FTB with a maximum of $100 million. Upon receipt of certification from the seller, the credit is allocated on a first-come, first-serve basis. The credit must be claimed on a timely filed original return. The determination by FTB with respect to the date a certification is received, and whether a return has been timely filed, may not be reviewed in any administrative or judicial proceeding. Any disallowance of a credit claimed on the basis of exceeding the $100 million limitation is treated as a mathematical error and any tax resulting from such disallowance may be assessed in the same manner as applicable to mathematical errors. The newly enacted state law remains in effect until December 1, 2013, and is repealed as of that date.

PROGRAM BACKGROUND

As of July 3, 2009, FTB stopped accepting new home credit applications and as of August 31, 2009, the entire $100 million in principal residence credits had been allocated.

THIS BILL

This bill would clarify that taxpayers that purchased a qualified principal residence prior to July 3, 2009, would be allocated the credit if the certification was submitted to FTB within one week before or after the close of escrow. This bill would also expand the availability of the principal residence credit to taxpayers who purchase a qualified principal residence on and after the effective date of this bill and before March 1, 2010.

In addition, this bill would require for each certification received from the seller the total amount of credit available for allocation be reduced by 70 percent of the credit allocated to the taxpayer. The credit may be allocated if the qualified principal residence was purchased prior to July 3, 2009, and the taxpayer submitted their certification for the home purchase credit within one week before or after the close of escrow but received by FTB not later than July 2, 2009.

For example, under this bill the 70 percent rate would be applied as follows, a taxpayer could be allocated a $10,000 credit, but the total amount of credits available for allocation would be reduced by 70 percent of the credit allocated, or $7,000. Under this bill, additional taxpayers could be allocated the credit.

This bill would clarify for those taxpayers that purchase a principal residence after the date of enactment of this bill, this bill would specify that certification would be required to be submitted to FTB within one week after the close of escrow.

This bill includes language to appropriate $44,000 to cover the one-time department costs detailed in the “Fiscal Impact” discussion below.

LEGISLATIVE HISTORY

AB 765 (Caballero/Solorio, 2009/2010) is identical to this bill. AB 765 failed passage out of the Senate Revenue and Taxation Committee.

AB 902 (Torres, 2009/2010) would allow a maximum credit of $3,000 for the amounts paid or incurred by a taxpayer for a single purchase of foreclosed property that would be the primary residence for the taxpayer. This bill failed passage out of the Assembly Revenue and Taxation Committee.

SB 49 (Dutton, 2009/2010) would make substantive changes to the Qualified Purchase residence credit similar to this bill. SB 49 would eliminate the provision that would allow the taxpayer to reserve the credit and would eliminate the current aggregate allocation cap of $100 million. This bill failed passage out of the Senate Revenue and Taxation Committee.

SB 206 (Dutton, 2009/2010) would allow a maximum credit of $8,000 for a taxpayer that purchases a qualified principal residence on or after January 1, 2009, and before December 1, 2009. To qualify for the credit a taxpayer could not own a principal residence during the three-year period prior to the date of purchase. This bill failed passage out of the Senate Revenue and Taxation Committee.

SBX3 38 (Calderon, 2009/2010) would increase the credit limit from $100 million to $300 million and extend the operative period for the Qualified Principal Residence Purchase Credit from purchases made before March 1, 2010, to purchases made before December 1, 2010. This bill would also allow the taxpayer to reserve the credit prior to the close of escrow. This bill failed passage out of the Senate Revenue and Taxation Committee.

SBX 2 15 (Ashburn, Stats. 2009 Second Extraordinary Session, Ch. 11) allows a $10,000 credit for the purchase of a qualified principal residence for purchase made after March 1, 2009, and before March 1, 2010. The credit is being allocated by FTB with a maximum allocation of $100 million.

OTHER STATES' INFORMATION

Florida, Illinois, Massachusetts, Michigan, Minnesota, and *New York* laws do not provide a credit comparable to the credit allowed by this bill. The laws of these states were reviewed because their tax laws are similar to California's income tax laws.

FISCAL IMPACT

Staff estimates a combined one-time cost of approximately $44,000 (1 PY) to develop, program, and test revisions to existing systems for the revised credit limit and new applications received for the credit. Appropriation language has been included.[2]

[2] If this bill is enacted and no appropriation is provided to the department, the department would be required to redirect resources, which would have an adverse impact on current revenue generating programs and procedures

ECONOMIC IMPACT

Revenue Estimate

Estimated Revenue Impact of SBX3 37 As Amended October 14, 2009 Effective For Purchases Made On or After March 1, 2009, and Before March 1, 2010 Assumed Immediate Enactment ($ in Millions)		
2009-10	2010-11	2011-12
-$14	-$11	-$6

Revenue Discussion

The revenue impact of this bill would depend on the number of taxpayers that purchase a new or previously unoccupied single-family home and are currently unable to apply for the Qualified Principal Residence Purchase Credit due to the credit's $100 million allocation limitation.

Based on data from the California Builder Association for 2008 and using the Department of Finance's growth projections for new home starts as a proxy for growth in new home sales, it is estimated that approximately 33,500 new homes will be sold during 2009 in California. To exclude investment purchases, because qualified purchases must serve as a taxpayer's primary residence, projected new home sales for 2009 are reduced by 5 percent to approximately 31,800 [33,500 x (1 - 5%)]. Next, because qualified purchases are limited to those made on or after March 1, total sales for 2009 are reduced by 17 percent (2 months ÷ 12 months) to approximately 26,400 [31,700 x (1 - 17%)].

Current law provides a 5 percent or $10,000 credit for qualified purchases up to $100 million in total credits. This equates to 10,000 purchases ($100 million ÷ $10,000 creditable amount).

This bill would allow FTB to issue additional credits by requiring that 70 percent of awarded credits be applied against the $100 million allowed under current law. Therefore, under this bill, $30 million would be available for additional credit requests ($100 million x 70%). This bill would allow approximately 4,285 additional purchases to qualify for the credit ($30 million ÷ $7,000 credit amount). The department would accept an additional 4,285 applicants, allocate $10,000 or $42.8 million ($10,000 x 4,285 applications) and apply a 70 percent usage rate, which would result in approximately $7,000 tax credit per taxpayer, to be used over three years. .

New home projections for 2009 are estimated to exceed 25,000; after subtracting the 10,000 purchases that are allowed under current law, the remaining 15,000 sales are anticipated to exceed the additional 4,285 purchases that would become eligible for the credit under this bill.

Beginning with the tax year of the purchase, current law requires that no more than one-third of credits generated be used in each of the three taxable years. For 2009, this reduces credits used to $10 million ($30 million ÷ 3 years). The figures in the chart have been adjusted to reflect the cash flow impact on a fiscal-year basis. The revenue loss for fiscal year 2009-10 includes additional credits allocated and used for tax year 2009 and altered estimate payments for credits available for the 2010 tax year.

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