Franchise Tax Board

ANALYSIS OF AMENDED BILL

Author:	Dutton	Analyst:	Angela Raygoza	Bill Number:	SB 49
Related Bills:	See Legislative History	Telephone:	845-7814	Amended Date:	April 14, 2009
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Qualified Principal Residence Purchase Credit

SUMMARY

This bill would allow the Qualified Principal Residence Purchase Credit to be reserved.

SUMMARY OF AMENDMENTS

The April 14, 2009, amendments would do the following:

- Allow the credit where close of escrow occurs after March 1, 2010, if taxpayer reserves a tax credit, as specified, and
- Remove the $100 million tax credit allocation cap.

PURPOSE OF THE BILL

According to author's office, the purpose of the bill is to encourage sales of previously unoccupied single-family residences.

EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective immediately upon enactment and specifically operative for agreements entered into on or after March 1, 2009, and before March 1, 2010.

POSITION

Pending.

ANALYSIS

FEDERAL/STATE 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.

Board Position:			Department Director	Date
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Newly enacted federal tax law provides a refundable tax credit for “first-time homebuyers” in the amount of the lesser of $7,500 or 10 percent of the home’s purchase price. The credit is phased out for individual taxpayers with adjusted gross income (AGI) between $75,000 and $95,000, or $150,000 and $170,000 for joint filers.[1] The credit applies to principal residences purchased after April 8, 2008, and before July 1, 2009.

The credit is recaptured under the terms of IRC 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.

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 applies to 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.

The tax credit is allocated by FTB with a maximum cap of $100 million. Upon receipt of certification from the seller, the credit is being allocated based 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.

THIS BILL

This bill would allow taxpayers to reserve a Qualified Principal Residence Purchase Credit prior to the close of escrow. To reserve the credit, the taxpayer and seller would be required to jointly sign and submit to FTB certification that the taxpayer and seller have entered into the agreement on or after March 1, 2009, and before March 1, 2010. FTB would be required to reserve the credit upon receipt of the certification. If the taxpayer reserves a credit, the close of escrow would not be required to occur before March 1, 2010.

This bill would deny the credit if the taxpayer fails, within one week prior to close of escrow, to provide certification that the residence was unoccupied .

This bill would also remove the $100 million limitation on the credit and the requirement for the credit to be allocated by FTB on a first-come, first-served basis.

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[1] Adjusted Gross Income, as defined by IRC 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.

IMPLEMENTATION CONSIDERATIONS

This bill uses a term that is undefined, i.e., “agreement.” The absence of definitions to clarify this term could lead to disputes with taxpayers and would complicate the administration of this credit.

This bill adds language that would conflict with newly enacted law by allowing a credit reservation where the close of escrow does not have to occur before March 1, 2010. Because this bill lacks a specific cut-off date for this provision, taxpayers could enter into a contract before March 1, 2010, to buy a house built in 2012. If this is not the author’s intent, it is recommended the bill be amended to provide a specific period when the close of escrow should occur when a taxpayer provides a credit reservation.

Under existing law, there is a $100 million cap on the total credits FTB may allocate. It is unclear in this bill if taxpayers that were previously denied the credit because the maximum cap was reached could be allocated the credit. If the author’s intent is to allow previously denied taxpayers to receive a credit allocation, it is recommended the bill be amended to clarify how denied taxpayers would apply for the credit.

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

Implementing this bill would not significantly impact the department’s programs and operations.

ECONOMIC IMPACT

Revenue Estimate

This bill would result in the following revenue losses:

Estimated Revenue Impact of SB 49 Effective For Purchases Made On or After March 1, 2009, and Before March 1, 2010 Enactment Assumed After June 30, 2009 ($ in Millions)		
2009-10	2010-11	2011-12
-$18	-$20	-$18

This estimate 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 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. As of April 29, 2009, 4,880 applications totaling $47.4 million in credits were submitted to the department.

Based on historical data from the California Builder's Association for 2008 and using the Department of Finance's growth projections for 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 would be reduced by 5 percent to approximately 31,800 [33,500 x (1- 5%)]. Because qualified purchases are limited to those made after March 1, 2009, total sales for 2009 would be reduced by approximately 17 percent (2 months /12 months) to approximately 26,400 [31,800 x (1-17%)].

Existing law provides a 5 percent or $10,000 credit for qualified purchases up to $100 million in total credits. This equates to approximately 10,000 purchases ($100 million / $10,000 creditable amount). This bill would remove the credit allocation limit of $100 million, which would allow an estimated additional 16,400 purchases to qualify for the credit (26,400 – 10,000 number of credits allowed under current law).

For taxable year 2010, it is estimated that 8,099 new homes would be sold. To exclude investment purchases, because qualified purchases must serve as a taxpayer's primary residence, projected new home sales for 2010, those made before March 1st, 2010, would be reduced by 5 percent to approximately 7,700 [8,099 x (1- 5%)]. This was derived by using the same methodology outlined above and includes an increase for taxpayers that are anticipated to reserve the credit prior to the close of escrow.

Total credits generated during taxable year 2009 are estimated to total approximately $164 million (16,400 purchases x $10,000 credit amount). To determine the value of credits used to reduce taxes, taxpayers without a tax liability were excluded. It is assumed that one-third of the homebuyers who will receive certification for the credit do not have a tax liability, reducing credits available for use to approximately $109 million [$164 million x (1 - 33%)].

Starting with the taxable year of the purchase, this bill requires that no more than one-third of credits generated be used in each of the three taxable years. For 2009, this reduces available credits for use to approximately $36 million ($109 million ÷ 3 years). Of this $36 million, it is assumed that taxpayers would have sufficient tax liability to use 38 percent of the available credits in each year. The revenue loss to the state from 2009 purchases is estimated to be approximately $14 million ($36 million x 38%) per year for three years. Using the same methodology for 2010 purchases, we estimate losses of $6 million per year for three years. The figures in the chart have been adjusted to reflect the cash flow impact on a fiscal-year basis. The revenue loss of $18 million for fiscal year 2009-10 includes $14 million in new credits applied to reduce taxable year 2009 liabilities and $4 million in reduced estimated payments for tax year 2010 liabilities.

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