STATE OF CALIFORNIA
Franchise Tax Board

Summary Analysis of Amended Bill

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Subject: Increased Exclusion on the Sale of a Principal Residence to First-Time Homeowners

Summary

This bill would, under the Personal Income Tax Law, increase the maximum amount of the income exclusion on the sale of a principal residence, when the buyer is a first-time homeowner.

Recommendation – No position.

Summary of Amendments

The May 10, 2018, amendments recast eligibility for the increased exclusion, added defined terms, and a certification requirement.

As a result of the May 10, 2018, amendments, all of the department's implementation and technical considerations discussed in the department's analysis of the bill as amended April 2, 2018, have been resolved.

Except for the “Reason for the Bill,” “This Bill,” “Implementation Considerations,” “Technical Considerations,” “Fiscal Impact,” and “Economic Impact” sections, the remainder of the department's analysis of the bill as introduced on April 2, 2018, still applies. The “Policy Concerns” section has been restated below for convenience and the “Support/Opposition” section has been updated to reflect currently available information.

Reason for the Bill

The reason for the bill is to provide an incentive to owners of California principal residences to sell their property to first-time homeowners by increasing the maximum income tax gain exclusion.

This Bill

This bill would, on or after January 1, 2018, increase the seller’s maximum excludable gain on the sale of a principal residence from $250,000 to $300,000 for individuals, and from $500,000 to $600,000 for joint return filers and surviving spouses, for the sale of a qualified principal residence to a certified qualified first-time homeowner.

For purposes of the increased exclusion, this bill would define the following terms:

"Qualified first-time homeowner" would mean any individual (and, if married, that individual's spouse) who had no ownership interest in a principal residence during the preceding three-year period ending on the date of the purchase of the qualified principal residence. For this purpose, a qualified first-time homeowner does not include any individual, his or her spouse, or both, if they are treated as a "related party" to the seller.

"Qualified principal residence" would mean a single-family residence, whether detached or attached, that is purchased to be the principal residence of a qualified first-time homeowner for a minimum of two years and is eligible for the homeowner's exemption under Revenue and Taxation Code section 218.

The increased exclusion would be allowed subject to the seller obtaining from the buyer on or before the closing date of the sale or exchange of the qualified principal residence, a written certification that includes all of the following:

- The buyer's name, taxpayer identification number, and address;
- The seller's name, taxpayer identification number, and address;
- The address and sales price of the qualified principal residence; and
- An affirmative representation by the buyer which verifies he or she meets the requirements to be a qualified first-time homeowner, including a representation that the buyer has not owned a qualified principal residence during the three-year period ending on the closing date of the purchase of the qualified principal residence.

Fiscal Impact

The department's costs to implement this bill have yet to be determined. As the bill moves through the legislative process, costs will be identified.

Economic Impact

Revenue Estimate

This bill would result in the following revenue loss:

Estimated Revenue Impact of SB 1116 as Amended May 10, 2018
For Taxable Years Beginning On or After January 1, 2018
Assumed Enactment after June 30, 2018

($ in Millions)

Fiscal Year	Revenue
2018-2019	- $130
2019-2020	- $75
2020-2021	- $75

Revenue Discussion

This revenue estimate is based on a proration of the Joint Committee on Taxation (JCT) federal tax expenditure estimate for the exclusion of capital gains on sales of principal residences. In January 2017, the JCT estimated the federal revenue impact of the exclusion to be $33 billion in federal fiscal year 2019.

To determine California's share of the federal loss, California Association of Realtors (CAR) and National Association of Realtors data was used to calculate that 19 percent of dollar volumes for homes sales are attributable to California, then federal and state capital gains tax rates were analyzed to estimate a federal/state tax adjustment of 60 percent,[1] or $3.8 billion.

Using data from the CAR, it was determined that 35 percent of home sales are to first-time homeowners. Of the sales to first-time homeowners, it is estimated that there would be a five percent increase in the amount excluded, resulting in an estimated revenue loss of $65 million in taxable year 2018.

The tax-year estimates are converted to fiscal-year estimates and rounded to arrive at the amounts shown in the above table.

Support/Opposition[2]

Support: Orange County Realtors (sponsor).

Opposition: None provided.

Policy Concerns

This bill would create differences between federal and California tax law, thereby increasing the complexity of California tax return preparation.

This bill lacks a sunset date. Sunset dates generally are provided to allow periodic review of the effectiveness of a tax benefit by the Legislature.

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[1] Adjustment based on tax rate prior to the enactment of the Tax Cuts and Jobs Act of 2017 (P.L. 115-97).
[2] Senate Governance and Finance Committee Analysis dated May 4, 2018.