Franchise Tax Board **SUMMARY ANALYSIS OF AMENDED BILL**

Author:	Galgiani	Analyst:	Jon Feenstra	Bill Number:	SB 434
Related Bills:	See Prior Analysis	Telephone:	845-4870	Amended Date	April 6, 2017
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SUBJECT: Mortgage Forgiveness Debt Relief

SUMMARY

This bill would extend the state exclusion of mortgage forgiveness debt relief for three years, to generally apply to discharges occurring in 2014, 2015, and 2016.

RECOMMENDATION – NO POSITION

SUMMARY OF AMENDMENTS

The April 6, 2017, amendments reduced the total amount of debt forgiveness that may be excluded from gross income for discharges occurring in 2014, 2015, and 2016. Except for the "This Bill" and "Economic Impact" sections, the remainder of the department's analysis of the bill as introduced on February 15, 2017, still applies. The "Fiscal Impact" section has been restated below for convenience.

THIS BILL

This bill would extend California's modified conformity to mortgage forgiveness debt relief for three years, generally through 2016. Specifically:

- The California exclusion would be extended to generally apply to discharges occurring on or after January 1, 2014, and before January 1, 2017,[1]
- The maximum amount of qualified principal residence indebtedness would be $800,000 ($400,000 in the case of a married/Registered Domestic Partner (RDP) individual filing a separate return),
- The total amount excludable from gross income would be limited to $250,000 ($125,000 in the case of a married/RDP individual filing a separate return), and
- No penalties or interest would be imposed with respect to discharges occurring in the 2014, 2015 or 2016 taxable years.

[1] California would additionally conform, with its modifications and limitations, to the federal provision that provides for an exclusion from gross income in the case of those taxpayers whose qualified principal residence indebtedness is discharged on or after January 1, 2017, if the discharge is pursuant to an arrangement entered into and evidenced in writing prior to January 1, 2017.

FISCAL IMPACT

This bill would not significantly impact the department's costs.

ECONOMIC IMPACT

Revenue Estimate

This bill would result in the following revenue loss:

Estimated Revenue Impact of SB 434 As Amended April 6, 2017 Assumed Enactment After June 30, 2017 ($ in Millions)		
2016-17	2017-18	2018-19
- $75	- $60	- $3.1

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

Revenue Discussion

This estimate is based on a proration of the Joint Committee on Taxation's (JCT's) estimated revenue effects of the Tax Increase Prevention Act of 2014 (Public Law 113-295) and the Protecting Americans From Tax Hikes Act of 2015 (Division Q of Public Law 114-113), for the extensions of federal mortgage forgiveness debt relief made by those Acts; the JCT estimates the revenue impact for the three-year period of those extensions to be a loss of $8.3 billion (generally for discharges occurring in tax years 2014, 2015, and 2016).[2] The prorated loss for California would be approximately $130 million for the three year exclusion.

To determine California's prorated amount of the federal loss, the federal estimate is reduced to reflect California's approximate 15 percent share of the national housing market, then reduced by 65 percent to account for the differences between federal and state law of the allowable amounts of acquisition indebtedness and the limitation on the amount excludable from income, and finally reduced by an additional 70 percent to reflect the differences between federal and state tax rates, resulting in an estimated loss of $130 million.

[2] The federal estimated loss includes allowing an exclusion from gross income for those taxpayers whose qualified principal residence indebtedness is discharged on or after January 1, 2017, if the discharge is pursuant to an arrangement entered into and evidenced in writing prior to January 1, 2017.

It is estimated that the prohibition of interest and penalties on discharges would result in an additional loss of $5 million, which is calculated by assuming that approximately 25 percent of the total amount that would be excluded from gross income by this bill would have been reported as income on tax returns filed by taxpayers who were unable to pay the tax attributable to that income when the returns were filed.

Due to the assumed enactment date, this bill would affect taxpayers who have filed prior-year returns. Because these taxpayers would file amended returns, amounts from such returns are accrued back one year.

The total estimated loss is converted to fiscal years and then rounded to arrive at the amounts shown in the above table.

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