DEPARTMENT OF FINANCE
OFFICE OF THE DIRECTOR

EDMUND G. BROWN JR. GOVERNOR

STATE CAPITOL ■ ROOM 1145 ■ SACRAMENTO CA ■ 95814-4998 ■ WWW.DOF.CA.GOV

Honorable John M Moorlach
Member of the Senate
State Capitol, Room 2048
Sacramento, CA 95814

Dear Senator Moorlach:

Our office has reviewed SB 1116 as amended May 10, 2018. On the basis of our attached analysis of available information, we regret that we must oppose your legislation. If you feel that we may have overlooked factors that may be important in evaluating your legislation, please call me at 445-8610 and we will arrange any assistance necessary.

Sincerely,

For

MICHAEL COHEN
Department Director

Attachment

DEPARTMENT OF FINANCE BILL ANALYSIS

AMENDMENT DATE: 05/10/2018
POSITION: Oppose

BILL NUMBER: SB 1116
AUTHOR: Moorlach, John M

BILL SUMMARY: Personal income taxes: exclusion: capital gains: sale of residence.

This bill increases the Home Sale Gain Exclusion for sellers who sell to first-time homeowners from $250,000 to $300,000 for individual taxpayers, and from $500,000 to $600,000 for taxpayers who file joint, head of household, or surviving spouse.

FISCAL SUMMARY

The Franchise Tax Board (FTB) estimates total revenue losses of $130 million in 2018-19, $75 million in 2019-20, and $75 million in 2020-21.

The FTB's administrative costs have not yet been determined.

This bill imposes a state-mandated local program by expanding the scope of the crime of perjury. However, Finance does not believe that this creates a reimbursable state mandate because costs incurred by local agencies as a result of this bill are not new and do not require a higher level of service to be provided.

COMMENTS

The Department of Finance is opposed to this bill for the following reasons:

- This bill results in substantial revenue losses.
- Much of this bill's benefit is likely to go to higher-income individuals that benefit from the higher capital gains exclusion.
- Existing law provides tax deductions for many home-buying expenses and home-ownership costs, and programs from the California Housing Finance Agency help first-time home buyers with down payment assistance.
- Policy changes that lead to an increase in the housing supply are the most effective long-term solution for reducing housing costs for all Californians, and this bill does not address the issue of the shortage of housing.

ANALYSIS

1. Programmatic Analysis

   Under current federal and state law, gross income means all income derived from any source (e.g., wages, interest, dividends, prizes, etc.), except for those items that are specifically excluded by statute. In general, California conforms to most federal gross income exclusions by reference to the

Analyst/Principal	Date	Program Budget Manager	Date
R. Finnestead		Irena Asmundson	

Department Deputy Director — Date
Orig. Signed By J. Onodera MAY 21 2018

Governor's Office: By: Date: Position Approved______
Position Disapproved______

ANALYSIS (continued)

federal Internal Revenue Code, which means that an item is included under both laws, unless a specific exemption is provided for in California law.

Current federal law excludes gains from the sale or exchange of property if, during the five-year period ending on the date of the sale or exchange, such property has been owned and used by the taxpayer as the taxpayer's principal residence for periods aggregating two years or more. The amount of gain excluded from gross income with respect to any sale or exchange of a principal residence is limited to $250,000 for individuals. The exclusion from gain of sale for married taxpayers filing jointly increases to $500,000.

California state law conforms to federal law in regards to excluding gains from the sale or exchange of property.

This bill increases the maximum excludable amounts in the event that the seller's principal residence is sold to a first-time home-buyer from $250,000 to $300,000 for individual taxpayers, and from $500,000 to $600,000 for joint filers and surviving spouse taxpayers.

This bill defines a "qualified first-time homeowner" as someone 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.

This bill defines "qualified principal residence" as 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.

This bill requires that the seller obtains a certificate, in writing, that the buyer is a qualified first-time home-buyer. The seller must provide the FTB with the following information from the buyer:

- 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.
- An affirmative representation by the buyer which verifies 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.

Discussion

A background sheet provided by the author's office states, "California is in the midst of a severe housing supply shortage. With the median sales price at $522,440, only 32% of Californians can afford a median priced home...SB 1116 provides a small incentive to encourage a sale to our younger residents that are just starting out in life, thus making homeownership attainable for working Californians."

The California Department of Housing and Community Development states in their 2018 report on housing that one of the major challenges facing California is a lack of production, with actual building falling short of projected needs. The Public Policy Institute of California states in their 2018 report on California housing that restrictive zoning and land use policies depress California housing supply and

BILL ANALYSIS--(CONTINUED) **Form DF-43**

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ANALYSIS (continued)

increase housing costs. This bill does not address this lack of supply or housing affordability.

The Governor's Budget included $4.4 billion in state and federal funding across various departments and programs to develop affordable housing, provide assistance to first-time home buyers, and offer various supports for individuals experiencing homelessness. In addition, there are existing tax incentives already in place for homeowners. Tax preferences for homeownership include: mortgage interest deductibility for the first and second home, deductibility from income of property taxes, deductibility of certain capital gains on the sale of a home, and deductibility of interest payments on a home improvement loan.

Generally, conformity with federal law is good state tax policy as it eases administration and is easier for taxpayers. This bill will put California out of conformity with federal law, as the capital gains exclusion from income would increase on state income taxes but not on federal income taxes.

	SO	(Fiscal Impact by Fiscal Year)							
Code/Department	LA	(Dollars in Thousands)							
Agency or Revenue	CO	PROP							Fund
Type	RV	98	FC	2017-2018	FC	2018-2019	FC	2019-2020	Code
1730/FTB	SO	No	U	--	U	--	U	--	0001
4116200/Personal I	RV	Yes	U	--	U	-130,000	U	-75,000	0001