STATE OF CALIFORNIA
Franchise Tax Board

Bill Analysis

Author: Ochoa Bogh | Sponsor: | Bill Number: SB 601

Related Bills: See Legislative History | Amended: April 22, 2021

SUBJECT

Increase Capital Gain Exclusion for Sale of a Principal Residence to First-Time Homeowners

SUMMARY

This bill would, under the Personal Income Tax Law (PITL), 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 April 22, 2021, amendments resolved all of the department's technical considerations by accepting the amendments suggested in the department's analysis of the bill as introduced on February 18, 2021, created an additional implementation consideration, made clarifying changes, and added reporting requirements.

REASON FOR THE BILL

The reason for the bill is to provide an incentive to owners of principal residences to sell their property to first-time homeowners by increasing the maximum amount of gain excluded from gross income.

ANALYSIS

This bill would, on or after January 1, 2021, and before January 1, 2026, increase the seller's maximum excludable gain on the sale of a principal residence that may be excluded from gross income from $250,000 to $300,000 for single filers, 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 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 property tax exemption under Revenue and Taxation Code (RTC) 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 that the buyer 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.

To meet the requirements of Section 41 of the RTC, the bill states that the goals, purposes, and objectives of the increased exclusion from gross income would be to help level the playing field for first-time homebuyers and to get more first-time homebuyers into homes. The number of taxpayers utilizing the increased exclusion would be used to measure the effectiveness of credit.

This bill would require the Legislative Analyst Office (LAO) to collaborate with the Franchise Tax Board (FTB) to review the effectiveness of the increased exclusion from gross income. The review would include analysis of the demand and the economic impact of the increased income exclusion.

This bill would allow the LAO to request and the FTB to provide any information necessary to review the effectiveness of the increased exclusion from gross income. Any information provided that has not otherwise been made public would remain confidential taxpayer information prohibited from disclosure. The LAO would be required to publish the finding of the review by December 1 of an unspecified year.

Effective/Operative Date

As a tax levy, this bill would be effective immediately upon enactment and specifically operative for taxable years beginning on or after January 1, 2021, and before January 1, 2026.

Federal/State Law

Federal Law

Gross income means all income from whatever source derived, including gains from dealings in property, unless specifically excluded.

Gain from the sale or exchange of property is excluded from gross income 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.

Limitation

The amount of gain excluded from gross income with respect to any sale or exchange of a principal residence is limited to $250,000.

In the case of taxpayers who file a joint return for the tax year of the sale or exchange of the property, the $250,000 limitation (described above) that applies to the exclusion of gain from the sale or exchange of a principal residence becomes $500,000 if:

- Either spouse meets the ownership requirements with respect to the property;
- Both spouses meet the use requirements with respect to the property; and
- Neither spouse is ineligible for the benefits of the exclusion with respect to the property because of the one sale every two years rule.

A surviving spouse may exclude from gross income up to $500,000 of the gain from the sale or exchange of a principal residence owned jointly with a deceased spouse if the sale or exchange occurs within two years of the death of the spouse.

State Law

California imposes an income tax on the entire taxable income of residents of this state. Nonresidents of California must include income from sources within this state, including gains realized from the sale or transfer of property located within this state.

California conforms, under the PITL, to Internal Revenue Code (IRC) section 61, relating to gains from dealings in property, and to IRC section 121, relating to exclusion of gain from the sale of principal residence, as of the “specified date” of January 1, 2015, with modifications unrelated to the provisions of this bill.

Under RTC section 41, legislation that would create a new tax expenditure, which includes a credit, deduction, exclusion, exemption, or any other tax benefit as provided for by the state, is required to include specific goals, purposes, objectives, and performance measures to allow the Legislature to evaluate the effectiveness of the tax benefit.

Implementation Considerations

None noted.

Technical Considerations

None noted.

Policy Considerations

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

LEGISLATIVE HISTORY

SB 1116 (Moorlach, 2017/2018), substantially similar to this bill, would have, under the PITL, increased the maximum amount of the income exclusion on the sale of a principal residence, when the buyer is a first-time homeowner. SB 1116 did not pass out of the Senate Committee on Appropriations.

AB 1806 (Hagman, 2009/2010), would have provided conformity to the federal capital gain exclusion from gross income on the sale of a personal residence by a surviving spouse. AB 1806 did not pass out of the Assembly Revenue and Taxation Committee.

SB 401 (Wolk, Chapter 14, Statutes of 2010) changed the specified date from January 1, 2005, to January 1, 2009, for taxable years beginning on or after January 1, 2010, which among other things, conformed to federal law that allows surviving spouse to exclude from gross income up to $500,000 of the gain from sale of principal residence if the sale occurs within 2 years of the death of the spouse.

SB 1416 (Walters, 2009/2010) would have provided an exclusion from gross income, without limitation, for gain on the sale or exchange of a principal residence by a taxpayer 65 years or older. SB 1416 did not pass out of the Senate Revenue and Taxation Committee.

PROGRAM BACKGROUND

None noted.

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 601 as Introduced February 18, 2021, and Amended April 22, 2021.
Assumed Enactment after June 30, 2021

($ in Millions)

Fiscal Year	Revenue
2021-2022	-$120
2022-2023	-$80
2023-2024	-$85

This analysis does not account for changes in employment, personal income, or gross state product that could result from this bill or for the net final payment method of accrual.

LEGAL IMPACT

None noted.

APPOINTMENTS

None noted.

SUPPORT/OPPOSITION

To be determined.

ARGUMENTS

To be determined.

LEGISLATIVE CONTACT

FTBLegislativeServices@ftb.ca.gov