SENATE RULES COMMITTEE SB 601

Office of Senate Floor Analyses

(916) 651-1520 Fax: (916) 327-4478

THIRD READING

Bill No: SB 601

Author: Ochoa Bogh (R), et al.

Amended: 5/20/21

Vote: 21

SENATE GOVERNANCE & FIN. COMMITTEE: 4-0, 5/6/21

AYES: McGuire, Nielsen, Hertzberg, Wiener

NO VOTE RECORDED: Durazo

SENATE APPROPRIATIONS COMMITTEE: 7-0, 5/20/21

AYES: Portantino, Bates, Bradford, Jones, Kamlager, Laird, Wieckowski

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SUBJECT: Personal income taxes: exclusions: capital gains: sale of residence

SOURCE: Author

DIGEST: This bill increases the current exclusion from income for taxpayers who sell their primary residence to a qualified first-time homeowner.

ANALYSIS:

Existing law:

1) Allows various income tax credits, deductions, exemptions, and exclusions. The Legislature enacts such tax incentives either to compensate taxpayers for incurring certain expenses, such as child adoption, or to influence certain behavior, such as charitable giving. The Legislature uses tax incentives to encourage taxpayers to do something that but for the tax credit, they would otherwise not do.

2) Defines gross income as all income regardless of source, unless specifically exempted.

3) Allows an exclusion from income for the sale of a primary residence, which allows taxpayers to exclude the capital gain from the sale of their primary

residence. To qualify for the exclusion, taxpayers must have lived in their home for at least two of the last five years. The gain is limited to the following amounts:

a) $250,000 for taxpayers who are single or married filing separately; and

b) $500,000 for taxpayers who are married filing jointly or surviving spouses who sell their home within two years of their spouse's death.

This bill:

1) Increases the current exclusion from income for taxpayers who sell their primary residence to a qualified first-time homeowner, as defined. The bill increases the exclusion to the following amounts:

   a) $300,000 for taxpayers who are single or married filing jointly; and

   b) $600,000 for taxpayers who are married filing separately, a head of household, or a surviving spouse.

2) Defines a "qualified first-time homeowner" as 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 closing date of the purchase of the qualified principal residence. Qualified first-time homeowner does not include any individual, their spouse, or both, if the individual and their spouse are treated as a "related party," as defined in the Internal Revenue Code.

3) Defines a "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 and is eligible for the homeowner's exemption for property tax purposes.

4) Requires that on or before the closing date of the sale or exchange of the qualified residence, the seller obtains a certification from the buyer, in writing and signed under penalty of perjury, that the buyer is a qualified first-time homeowner. The certification shall include the following information in a form and manner as prescribed by the Franchise Tax Board.

   a) The buyer's name, taxpayer identification number, and address.

   b) The seller's name, taxpayer identification number and address.

   c) The address and sales price of the qualified principal residence.

   d) An affirmation representation by the buyer that the buyer meets the requirements provided under this section and 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.

5) Allows the increased exclusion for taxable years beginning on or after January 1, 2021 and before January 1, 2026.

6) Makes the measure's enactment contingent upon an appropriation in the annual Budget Act.

Background

California real estate market. California is in the midst of a housing crisis. According to a report in 2019 from the Legislative Analyst's Office (LAO) *Considerations for the Governor's Housing Plan*, "California home costs 2.5 times the national average. California's average monthly rent is about 50 percent higher than the rest of the country. High housing costs drive California's official poverty rate from roughly 13 percent (slightly higher than average) to 19 percent (highest in the nation) under the Census Bureau's Supplemental Poverty Measure, which takes into account food, clothing, shelter, and utilities." The Department of Finance announced, in April 2021, that the median price for a single family home reached $758,990 in California which represents a 24 percent increase from a year ago. This large increase makes it difficult for first time homebuyers to enter a very competitive market.

FISCAL EFFECT: Appropriation: No Fiscal Com.: Yes Local: Yes

According to the Senate Appropriations Committee, "The Franchise Tax Board indicates that this bill would result in General Fund revenue losses of $120 million in 2021-22, $80 million in 2022-23, and $85 million in 2023-24. FTB's implementation costs have yet to be determined."

SUPPORT: (5/21/21)

California Association of Realtors
Howard Jarvis Taxpayers Association
Inland Gateway Association of Realtors
Inland Valleys Association of Realtors
Livable California

OPPOSITION: (5/21/21)

California Federation of Teachers
California School Boards Association
California Tax Reform Association

ARGUMENTS IN SUPPORT: According to the author, "SB 601 is a step in the right direction towards leveling the playing field for first-time homeowners. It would do so by allowing homeowners who sell their homes to a first-time homebuyer to exclude capital gains of $300,000 for single filers instead of the current $250,000 maximum and $600,000 for joint filers instead of the current $500,000 maximum from their gross income. California is in the midst of a housing crisis. With the median price of a single family home being $693,690 in 2020 (more than twice the national average), an analysis done by the California Association of Realtors showed that only 28% of households could afford a home at this price. The cause of these high prices is mostly due to a severe lack of housing supply to meet increasing demand. One of the many consequences of this supply shortage is an extremely competitive market for potential home buyers, especially buyers looking to purchase their first home. In fact, California ranked as the toughest state in the nation for first-time home buyers according to a report done by bankrate.com. The report names a number of reasons for this ranking: the relatively high cost of housing, the tight market for available entry-level homes and the struggle that millennials face in saving for a down payment. Homeownership is the bedrock of the American dream. Too many young people are seeing this dream move further and further out of their reach due to the high cost of housing in California. SB 601 is one small step we can take towards making that dream more attainable for these hard working Californians."

ARGUMENTS IN OPPOSITION: According to the California Tax Reform Association, "While most efforts to incentive first-time home purchases provide a direct benefit to the buyers, this measure would instead disproportionately benefit wealth property owners, who already benefit from numerous programs to assist homeowners, such as Proposition 13. This, of course, in addition to the equity a property owner obtains upon the sale of their home. Effective tax exemption programs incentivize activity that otherwise would not have occurred. Because first time home buyers are highly motivated to purchase a home, and receive no direct benefit from this proposed program, it seems unlikely that this measure would result in a purchase that would have not otherwise occurred. Instead, this measure would cost the state General Fund millions of dollars which could have otherwise directly benefited those most in need of housing in the state."

Prepared by: Jessica Deitchman / GOV. & F. / (916) 651-4119
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