Date of Hearing: April 20, 2016

ASSEMBLY COMMITTEE ON HOUSING AND COMMUNITY DEVELOPMENT
David Chiu, Chair
AB 1736 (Steinorth) – As Amended March 10, 2016

SUBJECT: Personal income taxes: deduction: homeownership savings accounts

SUMMARY: Creates a "Homeownership Savings Account" (HSA) with account requirements and limitations similar to those governing Individual Retirement Accounts (IRAS). Specifically, **this bill**:

1) Excludes from gross income any income accruing to the HSA during the taxable years commencing on or after January 1, 2017.

2) Allows a deduction equal to the amount deposited in the HSA by a qualified taxpayer in any taxable year commencing on or after January 1, 2017, not to exceed:

   a) $20,000 for qualified taxpayers who are married filing a joint return, a head of household, and surviving spouses.

   b) $10,000 for qualified taxpayers filing a return other than those specified.

3) Provides that amounts may be withdrawn to pay for qualified homeownership expenses.

4) Specifies that any withdrawals for other than qualified expenses shall be included in income of the payee or distributee for the taxable year in which the payment or distribution is made unless the payment or distribution is used to pay for the homeownership savings expenses of a qualified taxpayer who established the account.

5) Defines "Homeownership Savings Account" as a trust that meets all of the following requirements:

   a) Is designated as a homeownership savings account by the trustee;

   b) Is established for the exclusive benefit of any qualified taxpayer establishing the account where the written governing instrument creating the account provides for the following:

      i. All contributions to the account are required to be in cash; and

      ii. The account is established to pay, pursuant to the requirements and limitations of this section, for the qualified homeownership savings expenses of a qualified taxpayer establishing the account.

   c) Is, except as otherwise required or authorized by this section, subject to the same requirements and limitations as an IRA established under Section 408 of the Internal Revenue Code, relating to individual retirement accounts, and any regulations adopted thereunder.

   d) Is the only homeownership savings account established by the qualified taxpayer.

6) Defines "Qualified homeownership expense" as expenses, including a down payment or closing costs, paid or incurred in connection with the purchase of a qualified taxpayer's principal residence in California for use by that taxpayer who established the homeownership savings account.

7) Defines "Qualifed taxpayer" as any individual, or individual's spouse, who had no present ownership interest in a principal residence during the preceding three-year period ending on the date of the purchase of the principal residence subject to the contribution allowed by this section.

8) Defines "Trustee" as defined under a traditional IRA.

9) Takes effect immediately as a tax levy.

EXISTING LAW:

1) Allows various deductions and exclusions in computing taxable income under the Personal Income Tax Law.

2) Provides that amounts held in a traditional IRA are generally included as income when withdrawn, except to the extent the withdrawal is a return of nondeductible contributions. Withdrawals are subject to an additional state tax of 2.5% if it is withdrawn prior to age 59, with some exceptions. Specifically, the taxpayer is not subject to the early withdrawal tax if the withdrawal is used for first-time homebuyer expenses of up to $10,000.

3) Specifies that the California Housing Finance Agency (CalHFA) provide down payment assistance in the form of deferred payment, low-interest; and junior mortgage loans which are designed to reduce principle and interest payments to make financing affordable for first time low and moderate income homebuyers. In most cases, CalHFA programs may be used in conjunction with other first-time homebuyer programs, including programs offered by nonprofit entities.

FISCAL EFFECT: Unknown

COMMENTS:

The most significant investment the state makes each year in housing is through the mortgage interest deduction on primary residences. The Franchise Tax Board (FTB) estimates that the impact of the mortgage interest deduction on state revenues for 2016-2017 will be $5 billion dollars. In addition to the mortgage interest deduction homeowners receive on their primary residence FTB estimates the mortgage interest deduction for second homes for 2016-2017 will result in an estimated $360 million in revenue loss. Funding for affordable housing production and programs to assist lower income families become homeowners has been largely eliminated in the past few years. Proposition 46 of 2002 and Proposition 1C of 2006 together provided $4.95 billion for affordable housing. These funds financed the construction, rehabilitation, and preservation of 57,220 affordable apartments, including 2,500 supportive homes for people experiencing homelessness, and over 11,600 shelter spaces. In addition, these funds have helped 57,290 families become or remain homeowners. Nearly all of these funds have been awarded.

The California Housing Finance Agency (CalHFA) operates the California Homeowner Downpayment Assistance Program (CHDAP) and provides homebuyers between 3% and 6% in downpayment assistance secured as a second mortgage on the home. The program operates as a revolving loan and when a home is sold CalHFA is repaid allowing the funds to go to another homebuyer. There is approximately $150 million available in CHDAP at this time. The program can provide downpayments to individuals that make up to 120% of the area median income (AMI) and just recently raised its income limits to 140% of AMI in high cost areas. CalHFA operates independently of the state General Fund and derives the funding for its downpayment assistance program from the sale of bonds.

This bill allows taxpayers to contribute $20,000 a year, for a married couple filing joint returns, and $10,000 for a single filers to a HSA. The contribution to the HSA is not subject to income taxes until the taxpayer withdrawal's the funds to use toward the purchase of a home. Taxpayers who have not owned a home within the last three years would be eligible for the HSA program.

Purpose of this bill: According to the author "California is in the midst of a housing crisis. There is a substantial lack of new home construction: according to the California Homebuilding Foundation, the number of annual housing permits in 2015 was similar to the slowest years in the 1980s and 1990s. This shortage is hitting the affordable and middle-class housing markets alike. AB 1736 allows Californians to utilize "Homeownership Savings Accounts" to save more of their own money for use on their first down payment and closing costs. While an increased supply of housing is needed, this bill will assist them in defraying the sizable costs of living in California and help empower them to achieve homeownership in the near term."

Agreements in support: According to the Building Industry Association, data recently released by Beacon Economic shows California ranks 49th in homeownership and last in overall housing affordability. "While an average California home cost $440,000, homebuyers need additional tools to attain the American Dream. As the state grapples with a housing affordability crisis, AB 1736 will allow first-time homebuyers to save more of their own money in order to attain the benefits of homeownership."

Arguments in opposition: According to the California Tax Reform Association, "this bill provides little or no help to those struggling to buy a home in California's expensive housing market. By allowing a deduction, it provides the greatest benefits to those who are better off, that is, are in the higher tax brackets in our progressive tax system. In fact, since it has no income limitation it merely provides a tax shelter for those with substantial income, but even with such a limitation it would still provide disproportion benefits to the well-off who can save the most and are at least in need of help in buying a home. "

Staff comments:

Unlike CHDAP the funding for this program would come from a reduction in state revenues and would be a one-time investment in one individual rather than function as a revolving loan fund. The committee may wish to consider if this is the right investment considering the affordable housing challenges facing the state. The committee may wish to consider whether there should be some income limitation on those who can qualify for a HSA to focus this bill on lower income individuals.

The potential revenue loss to the state as a result of this bill are unclear. Should this bill pass out of this committee it will be referred to the Committee on Revenue and Taxation who can determine the cost. The author has indicated a willingness to amend this bill to reduce the cost by revising how and when taxes can be applied to the HSA. The committee may wish to request that the author address those issues in the Committee on Revenue and Taxation.

Committee amendments:

The committee may wish to consider the following amendments:

- Only allow taxpayers that make up to 80% of area median income (AMI) qualify to create a HSA. If a taxpayer's income exceeds 80% AMI in any given year they cannot contribute to the HSA.

- Change the definition of "first time homebuyers" from taxpayers that have not owned a home within the last three years to a taxpayer who has never owned a home.

Double referred: If AB 1736 passes this committee, the bill will be referred to the Committee on Revenue and Taxation.

REGISTERED SUPPORT / OPPOSITION:

Support

California Association of Community Managers
California Association of Realtors
California Building Industry Association
California Counsel for Affordable Housing
California Credit Union League
County of San Bernardino
Educational Community for Homeowners
Housing Authority of the County of San Bernardino
League of California Cities
Silicon Valley Leadership Group
Western Manufacturing Housing Communities Association

Opposition

California Tax Reform Association

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