

LEGISLATIVE FISCAL OFFICE
Fiscal Note



Fiscal Note On: **HB 50** HLS 162ES 77
 Bill Text Version: **ORIGINAL**
 Opp. Chamb. Action:
 Proposed Amd.:
 Sub. Bill For.:

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|--|---------|-------------------------------|
| Date: June 6, 2016 | 8:31 PM | Author: MONTOUCET |
| Dept./Agy.: Revenue | | Analyst: Greg Albrecht |
| Subject: Income Tax Deduction For Net Capital Gains | | |

TAX/INCOME TAX OR +\$13,200,000 GF RV See Note Page 1 of 1
 Reduces the individual income tax deduction for net capital gains (Item #42)

Present law, for purposes of individual income taxation, allows a deduction of income from net capital gains, which shall be limited to gains recognized and treated for federal income tax purposes as arising from the sale or exchange of an equity interest in or substantially all of the assets of a nonpublicly traded corporation, partnership, limited liability company, or other business organization commercially domiciled in this state.

Proposed law limits this deduction to 50% of the qualified gains. Applicable to tax years beginning on and after January 1, 2016.

| EXPENDITURES | 2016-17 | 2017-18 | 2018-19 | 2019-20 | 2020-21 | 5 -YEAR TOTAL |
|---------------------|----------------|----------------|----------------|----------------|----------------|----------------------|
| State Gen. Fd. | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 |
| Agy. Self-Gen. | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 |
| Ded./Other | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 |
| Federal Funds | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 |
| Local Funds | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 |
| Annual Total | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 |

| REVENUES | 2016-17 | 2017-18 | 2018-19 | 2019-20 | 2020-21 | 5 -YEAR TOTAL |
|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|----------------------|
| State Gen. Fd. | \$13,200,000 | \$28,800,000 | \$30,000,000 | \$30,000,000 | \$30,000,000 | \$132,000,000 |
| Agy. Self-Gen. | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 |
| Ded./Other | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 |
| Federal Funds | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 |
| Local Funds | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 |
| Annual Total | \$13,200,000 | \$28,800,000 | \$30,000,000 | \$30,000,000 | \$30,000,000 | \$132,000,000 |

EXPENDITURE EXPLANATION

The Department of Revenue will incur some costs associated with preparing tax forms (hardcopy and online) for this change, as well as changes in tax instructions. These costs might be several thousand dollars of staff time for modifications and testing.

REVENUE EXPLANATION

According to the Department of Revenue data, the average amount of net capital gain deduction claimed over the five tax years of 2010 - 2014 has been some \$1.006 billion per year. Virtually all of this deduction is claimed on returns facing a 6% marginal tax rate. Thus, the average tax year liability reduction has been some \$60 million per year, and this bill will reduce this deduction and liability reduction by 50% or \$30 million.

The full effect of this liability change will occur over more than one fiscal year. According to Revenue Department data on returns filed claiming the net capital gains deduction, approximately 44% of the returns received by the end of a fiscal year were for the immediately preceding tax year, while 52% were for the second preceding tax, and 4% for the third preceding tax year. This approximate filing pattern is complicated by the relatively short time frame that the deduction has actually been taken on returns, and the federal capital gains tax rate increases in 2013 that distorted filings for that tax year. Applying that pattern to 50% 2016 liability estimate above results in a revenue gain in FY17 of \$13.2 million, then \$28.8 million in FY18, and \$30 million in FY19 and beyond.

Caution should be observed though given the volatile nature of any type of capital gains. A micro-simulation model of the state personal income tax, processing 2014 tax return data, indicates that this deduction reduces 2014 tax year liabilities by some \$76 million. Those liability reductions will be realized on returns filed in fiscal years 2015, 2016, 2017 and possibly even beyond. Thus, actual results from elimination of this deduction can vary significantly from year to year.

Senate Dual Referral Rules House

13.5.1 >= \$100,000 Annual Fiscal Cost {S&H}

6.8(F)(1) >= \$100,000 SGF Fiscal Cost {H & S}

13.5.2 >= \$500,000 Annual Tax or Fee Change {S&H}

6.8(G) >= \$500,000 Tax or Fee Increase or a Net Fee Decrease {S}

John D. Carpenter
Legislative Fiscal Officer