New Hampshire Department of Revenue Administration

Fiscal Note Quick Guide

19-0593

HB 686, *relative to calculating and funding the interim cost of an opportunity for an adequate education and extending the interest and dividends tax to capital gains.*

House Ways & Means

The proposed legislation extends the Interest and Dividends (I&D) Tax to capital gain income, and increases the exemption amounts. It is applicable to taxable periods ending on or after December 31, 2019.

Section 3 of the proposed legislation describes capital gain income which is taxable. It also repeals with section 13 the exemption with respect to capital distributions.

Section 8 of the proposed legislation increases the income exemption from $2,400 to $5,000, the 65 years of age or older exemption from $1,200 to $7,500, and the blind and disabled exemptions from $1,200 to $2,500.

Section 12 of the proposed legislation increases the filing threshold for individuals from $2,400 to $5,000, and for joint filers from $4,800 to $10,000.

Section 13 of the proposed legislation repeals the exemptions with respect to the sale or exchange of transferable shares, and capital distributions.

The amount of gross business profits attributable to capital gain income which is taxable or specifically exempted from taxation under the I&D Tax shall be deducted in determining taxable business profits under the Business Profits Tax (BPT), RSA 77-A.

The proposed legislation also adjusts the cost of providing the opportunity for an adequate education.

The fiscal impact is indeterminable but would likely increase revenues.

Although the fiscal impact is indeterminable, the Department has calculated a possible impact on revenues with respect to a single fiscal year based primarily on tax year 2016, with many assumptions. The Department estimates that the proposed legislation may increase revenues by $94,836,843, as follows: (1) the extension of the I&D Tax to capital gains may increase revenues by $108,334,440 (as described below*); and (2) the exemption increases may decrease revenues by $13,497,597. The Department used the following information to calculate the possible impact on revenues: tax year 2016 I&D Tax data as of 12/24/2018, and tax years 2015 and 2016 capital gains data as reported by the IRS on the NH Statement of Income (SOI) (for NH federal taxpayers).

It is important to note that $94,836,843 is for a single fiscal year, and that it does not take into account any possible changes in income, dividend, or capital gain income following tax year 2016.

It also does not take into account the effect of the proposed legislation on BPT revenues. Pursuant to RSA 77-A:4, I, income (including capital gain income) which is taxable or specifically exempted from taxation under the I&D Tax shall be deducted against the BPT. The proposed legislation, then, would make it so that a portion of the capital gain income that would currently be taxed at the BPT rate of 7.9% would instead be taxed at the I&D Tax rate of 5%. However, because we have no way of knowing which BPT taxpayers would also be required to pay I&D Tax on account of capital gains, we cannot estimate the impact except to say that it would decrease BPT revenues.

> ** The Department based its estimate on the assumption that the capital gain income that would be taxable under the I&D Tax would be similar to the net capital gain amount reported by the IRS on the SOI. Specifically, we reduced the net capital gain amount for every return contained within the SOI data with an adjusted gross income (AGI) of $1 or more and capital gain income by the proposed legislation's $5,000 income exemption. The result was estimated I&D Tax revenues from capital gain income of $108,334,440.*

Please note, the data used by the Department to calculate this estimate has several limitations, including the following:

- The Department has no way to limit the net capital gain income amount reported by the IRS on the SOI to taxpayers that would exceed the proposed legislation's $5,000 income exemption. It also has no way of knowing what other exemptions would be used to offset the I&D Tax revenues from capital gain income. Specifically, the SOI data used by the Department only contains individual income tax returns with an AGI of $1 or more; and it does not separate individuals from joint filers. It is likely that some portion of the returns (particularly those in the $1 to under $10,000 category) would not result in I&D Tax revenues, because they would not exceed the proposed legislation's $5,000 income exemption (or $10,000 for joint filers). However, without additional information, we make the assumption that all returns with an AGI of $1 or more would receive the $5,000 income exemption, which may underestimate the capital gain income that would be taxable under the I&D Tax. In contrast, we do not take into account the other possible exemptions, which may overestimate the capital gain income.
- The SOI data with respect to capital gains is a net amount, because, for federal income tax purposes, taxpayers may offset capital gains with capital losses (including in subsequent years). It should be noted that the proposed legislation would apply the I&D Tax to any net capital gains, but would not allow taxpayers a deduction/offset in any year with net capital losses.
- The SOI data contains capital gain flow-through income from non-NH partnerships and limited liability companies. They are not subject to the I&D Tax, but their members who are NH inhabitants may be subject to the I&D Tax.
- The SOI data contains capital gain flow-through income from S Corps, which are not subject to the I&D Tax. But NH inhabitants who receive S Corp distributions are subject to the I&D Tax.

Lastly, the Department would like to note the following items:

- The word "gross" was deleted all through section 2, presumably because the proposed legislation applies to *net* capital gain income. However, the word "gross" still applies to interest and dividend income. It should be preserved so that it does not have an effect on the current meaning of interest and dividend income.
- "Interest and Dividends" in current RSA 77:4-h was not amended to "Income," like in section 6 with respect to RSA 77:4-e.
- The applicability date in section 14 is inconsistent with the proposed legislation's overall applicability date for sections 2 to 13. It does not cover any taxable period ending after December 31, 2018 but before December 31, 2019. The correct applicability date is the "taxable period ending before December 31, 2019." Section 14 also seems unnecessary and potentially confusing. Pursuant to RSA 77:18, every taxpayer must pay "estimated tax for the subsequent taxable period," which, with respect to the proposed legislation, would include the estimated tax on capital gain income for taxable periods ending on or after December 31, 2019.
- The proposed legislation's applicability date means that it would likely become law in the middle of the taxable period (for calendar year filers). It does not allow sufficient time to notify taxpayers and for rulemaking.