New Hampshire Department of Revenue Administration

Fiscal Note Quick Guide

15-0365

HB 634-FN-A, *relative to applying the interest and dividends tax to trusts, increasing exemptions, and extending the tax to capital gains; and relative to homeowners property tax relief*

House Ways and Means Committee

This bill amends the Interest & Dividends ("I&D") Tax law, RSA 77, to make trusts taxable under the law, once again. This bill also changes the I&D Tax law to include the taxation of capital gains income. Capital gains reported on the taxpayer's federal income tax return that is equal to the positive sum of the net short-term capital gain or loss and the net long-term capital gain or loss reported shall be subject to the I&D Tax. Any capital gains income subject to taxation under the I&D tax shall be deducted under the Business Profits Tax (BPT) RSA 77-A.

The bill raises the I&D Tax thresholds and deductions from $2,400 to $5,000 for individuals, partnerships, limited liability companies, trusts, associations, executors and fiduciary filers; and raises from $4,800 to $10,000 for joint filers. Exemptions are increased from $1,200 to $2,500 for a taxpayer who is older than 65, blind and or disabled.

The bill establishes a Capital Gains Reserve ("CGR") Fund within the General Fund based on the tax collected from capital gains income. Under this bill, the Department of Revenue Administration (DRA) is required to make two calculations for I&D Taxes paid on capital gains tax revenue prior to September 30 each year. The comptroller will use the calculations provided by the DRA to transfer any excess revenue collected from capital gains tax revenue during the most recent fiscal year from the General Fund into the CGR Fund. If there is a deficit the comptroller shall transfer the difference from the CGR Fund to the General Fund, provided there are sufficient funds.

When the balance in the CGR Fund is in excess of an amount equal to 100% of the actual capital gain tax revenue for the most recently completed 3-year average annual amount, the bill requires the excess to be transferred into the stabilization reserve account.

The state treasurer will invest funds in the new CGR Fund. The interest earned shall be deposited as unrestricted General Fund revenue.

In addition, this bill also modifies the Low and Moderate ("L&M") Homeowners Property Tax Relief program to raise thresholds and increase the claimant's relief amount. The total household income is increased from $20,000 to $27,500 for a single person and from $40,000 to $55,000, if married or head of NH household.

The claimant's property threshold is raised from $100,000 to $130,000. Increasing the property thresholds also increases the percentage of property relief the claimant shall receive.

The amount distributed back to the towns and cities shall include $25,216,000 of revenue collected under the I&D Tax for capital gains income beginning July 1, 2016.

This bill would be effective July 1, 2015 and applicable to taxable periods ending after December 31, 2015.

Fiscal Impact Analysis

Capital Gains

The DRA estimated an increase in FY 2017 and each additional year forward in the amount of $91,614,593.15. This impact is calculated using Tax Year 2012 data. The DRA estimates an increase from net capital gains after deductions in the amount of $100,379,500, less the proposed changes increasing the filing thresholds, deductions, and exemptions equal to $8,764,906.85 for a total increase in revenue in the amount of $91,614,593.15.

More specifically:

- Increasing the threshold from $2,400 to $5,000 reduces revenues by $227,164.36.

- Increasing the threshold from $4,800 to $10,000 reduces revenues by $636,602.49 for a total reduction in revenues in the amount of $863,766.85.

- Increasing the deduction from $2,400 to $5,000 allows an increase in deductions in the amount of $40,924,000.

- Increasing the deduction from $4,800 to $10,000 allows an increase in deductions in the amount of $83,917,600.

- Increasing the exemptions from $1,200 to $2,500 allows an increase in exemptions in the amount of $33,181,200.

- The estimated total tax loss for the increased thresholds, deductions and exemptions would be $8,764,906.85.

- The DRA estimates that the capital gain income from NH residents would be similar to what is reported by the federal data on the NH Statement of Income (SOI). The SOI reports 123,020 NH individual income returns with net capital gains income for Tax Year 2012 in the amount of $2,622,840,000.

- For purposes of an estimate, the DRA assumes the SOI net capital gains income would be reduced by a minimum of one deduction in the amount of $5,000 per return for a total deduction amount of $615,250,000 (123,020 multiplied by $5,000 = $615,250,000).

- The net capital gain income of $2,622,840,000 reduced by the total deduction amount of $615,250,000 equals $2,007,590,000 multiplied by the current 5% I&D tax rate is an estimated $100,379,500 in newly generated I&D tax revenue.

The DRA, however, notes the following data and methodology weakness:

- The SOI data used is provided for AGI for individuals from $0 to $1,000,000 or more. The DRA is unable to limit the $2,622,840,000 to those who would meet the filing thresholds and what, if any, exemptions would be used.

- SOI data includes capital gain flow through income from non-NH partnerships that do not file an I&D return in NH.

- SOI data includes capital gain flow through income from s-corps. S-corps are not taxable under the I&D tax law; however, distributions from s-corps to NH inhabitants are subject to the I&D tax.

- SOI data for the capital gains is a net figure. For federal tax purposes, capital gains can offset capital losses. If in any one year, the maximum capital loss is in excess of $3,000, the balance of any additional loss over the $3,000 can be applied to subsequent years. This bill taxes a positive net gain on taxpayer's capital dispositions and does not provide a deduction if an individual or partner has a capital loss for that specified year.

- SOI data does not appear to capture capital gains received from non-NH taxpayers.

- When analyzing the data on the NH partnership BPT returns, capital gains reported totaled $6,751,469,742. This figure is a pre-apportionment amount. The information needed to determine the amount of capital gain/losses attributable to NH owners us unavailable.

- Any capital gains reported under BPT that are subject to tax under I&D will now be deducted from the BPT and taxed at a rate of 5% (I&D tax rate) instead of 8.5% (BPT tax rate). (3.5% difference)

Trusts

The DRA analyzed Tax Year 2012 data to estimate trust income adjusted for the new thresholds and increased deductions. The DRA, however, was unable to match the trust information to those trust beneficiaries who now file and pay the I&D Tax. Therefore, the DRA was unable to determine the difference between what the beneficiaries are currently filing and paying in I&D Tax and what the trusts that filed and paid in I&D Tax in Tax Year 2012.

Currently, every beneficiary from a trust that receives a distribution is allowed to offset that income by a deduction of $2,400 for an individual and $4,800 for joint filers. After the deduction is applied to the income the beneficiary can elect to take a $1,200 exception if they are older than 65, blind and or disabled.

L&M Program

The bill changes the current L&M relief for taxpayers in the following ways:

- increases both the single and married total household income allowed; and
- increases the amount of the value of the homestead that may be claimed as exempt.

The combined effects of these changes are indeterminable. The DRA anticipated there will be an increase in the number of allowed claims, as well as an additional approximate 30% increase in the total claims amount granted.

Assuming that the provisions of RSA 31-A:4 are not suspended in the coming biennial budget period; additional revenue flowing to municipalities would provide a reduction in local tax efforts. The limiting factor of revenue sharing in RSA 34-A:4 is a minimum of $47,300,000. The first $25,216,000 of revenue from capital gains taxes would become part of that revenue sharing amount.

Technical or Mechanical Issues

The DRA notes, as the bill is drafted, the phrase "[t]he capital gain reported on the taxpayer's federal income tax return…," appears to create a contradiction of the current treatment of interest and dividend income from a partnership (and other entities), which is based on the distribution (constructive receipt (unless subject to tax at the entity level) and not the amounts reported on the Schedule K-1.

In addition, the DRA also notes, that the two calculations required in Section 2 of the bill cannot be properly completed by the DRA prior to September 30. The DRA will not have the data needed to perform the calculations. I&D Tax filers who file on extension do not have to file their returns until November leaving September as an incomplete tax year.

Further, the DRA is unable to calculate the 3-year average annual amount of capital gain tax revenues collected because the DRA does not have the data available. The calculations are to be based on the tax collected from the capital gain income. It will be difficult for the DRA to ascribe the capital gains income to the taxable amount paid. Without a way for the DRA to ascribe the capital gains income to the taxable amount it is impossible for the DRA to estimate the average annual amount of revenue collected during the three fiscal years immediately prior to the most recently completed fiscal years for the tax on capital gains income. The DRA does not have the three previous years' data for all filers who may be subject to the new version of the tax. The DRA suggests that the legislation address the need for this information be provided by the taxpayer.

Finally, the DRA notes that the amount distributed back to the towns and cities shall include $25,216,000 of revenue collected under the I&D Tax for capital gains beginning July 1, 2016, but all I&D Tax monies will not have been received by July 1, 2016, making an inaccurate number distributed back to the towns. The DRA would recommend that the amount distributed back to the towns and cities shall include $25,216,000 of revenue collected under the I&D Tax for capital gains begin on July 1, 2017.

This bill could be administered by the DRA with an increase in expenditures that could be absorbed into the operating budget.