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Bill Analysis
Legislative Service Commission

H.B. 304
127th General Assembly
(As Introduced)

Rep. Driehaus

BILL SUMMARY

- Authorizes, for purposes of the personal income tax, the exclusion of income arising from a forgiven debt secured by a first mortgage on the taxpayer's principal residence.
- Authorizes the exclusion for taxable years beginning in 2008 but not for any taxable year beginning after 2012.

CONTENT AND OPERATION

Exclusion of qualified mortgage cancellation income

(R.C. 5747.01(A)(26))

Under the federal income tax, generally, when a creditor forgives a debt in whole or in part, the debtor must report the forgiven amount as income. (Internal Revenue Code section 61(a)(12).) A debtor need not report a forgiven debt as income, however, if immediately before and after the debt is forgiven the debtor is insolvent or if the debt has been discharged in a bankruptcy proceeding. (A debtor is insolvent when the debtor's debts exceed the fair market value of the debtor's assets.) (I.R.C. sec. 108.)

Currently, if a forgiven debt is required to be reported as income for federal income tax purposes it is also subject to taxation under the Ohio personal income tax.

The bill creates a limited exception to this rule for homeowners in foreclosure. The bill authorizes a taxpayer to exclude income recognized for the taxable year under the Internal Revenue Code arising from the discharge, in whole or in part, of indebtedness secured by a first mortgage on the taxpayer's principal residence. No deduction is allowed for the discharge of second or inferior mortgages or "home equity" loans.

Exclusion limitations

The amount of the bill's exclusion may not exceed the sum of (1) the outstanding amount of the debt (after application of the net proceeds from the sale of the principal residence), plus (2) the principal amount of any other debt secured by the principal residence.¹

The authorized exclusion is further limited to the amount of forgiven debt income attributable to the debtor's principal residence. "Principal residence" is defined as any dwelling owned and occupied by the taxpayer as a principal home (including a unit in a multi-unit dwelling or a manufactured or mobile home), and up to one acre of the land surrounding the home so long as the land is reasonably necessary for the use of the residence as a home. Thus, for example, if a debt is secured by a first mortgage on the taxpayer's principal residence and a mortgage on the taxpayer's surrounding farm, only the portion of the forgiven debt income relating to the taxpayer's principal residence may be excluded. Similarly, if the taxpayer's principal residence is surrounded by more than one acre of land, only the portion of the forgiven debt income relating to the residence, plus one acre, may be deducted. In either situation, it is unclear how such apportionment would be accomplished. The bill authorizes, but does not require, the Tax Commissioner to prescribe by rule the method for apportionment.

Affected taxable years

The deduction is authorized for taxable years beginning in 2008 but not for any taxable year beginning after December 31, 2012.

HISTORY

ACTION	DATE
Introduced	08-28-07

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¹ For federal tax purposes, the amount required to be reported as income for a secured forgiven debt is generally the outstanding amount of the debt minus the estimated fair market value of the collateral.