

BILL ANALYSIS AND FISCAL IMPACT REPORT
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March 7, 2017

Bill: SCORC Sub for SB-344

Sponsor: Senate Corporations and Finance Committee

Short Title: Income Tax Rates & Pre-K Funding

Description: This bill adds a new section to the Tax Administration Act titled Distribution-Income Tax-Public Pre-Kindergarten Fund and Children, Youth and Families Pre-Kindergarten Fund-Supplemental Public School State Equalization Guarantee Distribution. Distributions proposed are:

- Beginning July 1, 2019 and prior to July 1, 2020 a distribution is made to the public pre-kindergarten fund for early childhood care in an amount equal to seventy-five hundredths percent;
- Beginning July 1, 2020, a distribution shall be made to the public prekindergarten fund for early childhood care and education services provided for prenatal care through third grade in an amount equal to one and one-half percent;
- Beginning July 1, 2019 and prior to July 1, 2020, a distribution shall be made to the children, youth and families prekindergarten fund for early childhood care and education services provided for prenatal care through third grade in an amount equal to seventy-five hundredths percent;
- Beginning July 1, 2020, a distribution shall be made to the children, youth and families pre-kindergarten fund for early childhood care and education services provided for prenatal care through third grade in an amount equal to one and one-half percent;
- Beginning July 1, 2019 and prior to July 1, 2020, a distribution shall be made to the public school fund for the state equalization guarantee distribution, to supplement the non-categorical distribution, in an amount equal to four and one half percent;
- and beginning July 1, 2020, a distribution shall be made to the public school fund for the state equalization guarantee distribution, to supplement the non-categorical distribution, in an amount equal to three percent.

Section 32A-23-8 NMSA 1978 is amended to account for the above added distributions.

The bill amends Section 7-2-7 NMSA 1978 to add an upper tier for personal income tax (PIT).

- For married filing separate \$5,921 plus 6.4% of taxable income over \$125,000;
- For head of household, surviving spouses, and married individuals filing joint returns \$11,842 plus 6.4% of taxable income over \$250,000;
- For single individuals and estates and trusts, \$7,887.17 plus 6.4% of taxable income over \$166,666.67 ;

The bill also repeals an earlier version of Section 7-2-7 NMSA 1978. (being laws 2005 (1st S.S.) Chapter 3, Section 2).

Section 7-2-34 NMSA 1978 is also amended to set the deduction for net capital gain income for a taxable year equal to the taxpayers net capital gain income but not to exceed one thousand dollars (\$1,000) removing the percentages based on the taxable year subsections.

Effective Date: The effective date of the provisions of Sections 1 and 4 of this act is January 1, 2019. The provisions of Sections 2 and 3 of this act apply to taxable years beginning on or after January 1, 2018.

Estimated Revenue Impact*					R or NR**	Fund(s) Affected
FY2017	FY2018	FY2019	FY2020	FY2021		
\$-	\$-	\$(10,600)	\$(22,500)	\$(23,300)	R	Public Pre-K Fund
\$-	\$-	\$(10,600)	\$(22,500)	\$(23,300)	R	Children, Youth, & Families Pre-K Fund
\$-	\$-	\$(63,900)	\$(45,000)	\$(46,500)	R	Public School Fund
\$-	\$-	\$(35,600)	\$11,100	\$11,500	R	Net Contribution to General Fund

* In thousands of dollars. Parentheses () indicate a revenue loss. ** Recurring (R) or Non-Recurring (NR).

Methodology for Estimated Revenue Impact: The Taxation and Revenue Department (TRD) estimated the income tax impact using GenTax taxpayer data from the tax years 2010-2015. The new tax rate was applied to the new income thresholds; the revenue increase is the additional tax collected. The calculated revenue increase was estimated for future years using the consensus revenue estimating group (CREG) income tax growth rates. This section of the bill is effective January 1, 2018.

The savings from the capital gains cap was estimated using 2016 Tax Expenditure Report data. The number of claimants for the tax years 2013-2015 was multiplied by \$1,000 (the cap) and an average tax rate of 4.2% was applied. Approximately 96,000 taxpayers use the capital gains deduction each year. The additional contribution to the general fund is the estimated difference between what was claimed and the proposed cap. Future year savings were estimated using the CREG income tax growth rates. This section of the bill is effective January 1, 2018. This analysis assumes no taxpayers leave the state due to the tax increase.

FY2017	FY2018	FY2019	FY2020	FY2021	R or NR	Fund(s) Affected
\$-	\$-	\$30,400	\$62,100	\$64,300	R	Rate Increase Contribution to General Fund
\$-	\$-	\$19,100	\$39,000	\$40,300	R	Net Capital Gains Cap
\$-	\$-	\$49,500	\$101,100	\$104,600	R	Total Contribution to General Fund

The permanent distributions created by the bill have varying percentages of the net receipts of personal income tax. The permanent distributions to the Children, Youth and Families Pre-Kindergarten Fund, the Public School Fund, and the Public Pre-Kindergarten Fund begin July 1, 2019. The expense of the distributions – which reduce the general fund – was estimated using the December 2016 CREG forecast for personal income tax. Modifications to the forecast in out-years due to new revenue collections are part of the expenditure estimate.

Policy Issues: The income tax rate change implicates the tax principle of equity. The rates are distributed according to a taxpayer’s perceived ability to pay, and similarly situated taxpayers face similar tax burdens. Based on tax year 2014 data, approximately 64% of all PIT is paid by people who make more than \$75,000 in taxable income, while these people represent approximately 15% of total taxpayers. Approximately 62% of New Mexico PIT filers in lower income brackets pay approximately 5.5% of the total PIT revenues, whereas 40% of total New Mexico PIT filers have zero or less taxable income.

The capital gains deduction cap implicates this principle as well, but the \$1,000 cap represents a significant tax increase for approximately 96,000 taxpayers, spread across all income brackets. The capital gain deduction exists to incentivize savings and investment. This deduction is meant to encourage taxpayers to make investments and create wealth through those investments. Capping the benefit significantly reduces the cost of the expenditure.

Technical Issues: None.

Administrative & Compliance Impact: Minimal Impact. Several operating divisions of TRD will need to develop business processes to address various aspects of the bill. GenTax will need to be programmed, and coordination between the Information Technology Division and the Financial Services Bureau is required to ensure new distributions are properly established. Forms, instructions, publications, and software updates will be necessary in conjunction with annual tax year preparations.

Related Bills: