F I S C A L   I M P A C T   R E P O R T

ORIGINAL DATE 2/10/15
SPONSOR Trujillo, CH **LAST UPDATED** ______ **HB** 239

SHORT TITLE Repeal Capital Gains From Net Income **SB** ______

ANALYST van Moorsel

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY15	FY16	FY17	FY18	FY19		
$0.0	$0.0	$36,000.0-$54,000.0	$36,000.0-$56,000.0	$36,000.0-$58,000.0	Recurring	General Fund

(Parenthesis ( ) indicate revenue decreases

SOURCES OF INFORMATION
LFC Files

Responses Received From
Taxation and Revenue Department (TRD)

SUMMARY

Synopsis of Bill

House Bill 239 amends the Income Tax Act to repeal the deduction from net income of 50 percent of capital gains. Under current law, a taxpayer may deduct from his or her net income the greater of the taxpayer's net capital gain income for the taxable year, capped at $1,000.00; or 50 percent of the taxpayer's net capital gain income for the taxable year.

The provisions of the bill apply to taxable years beginning on or after January 1, 2016.

FISCAL IMPLICATIONS

TRD used historical data on the capital gains tax deduction over the last five tax years. TRD states that, over the last five years, the deduction has resulted in an average of $36 million in foregone general fund revenue. As such, TRD estimates this bill would result in a $36 million gain to the general fund, this is the lower bound of the range presented in the revenue table.

TRD points out the amount of capital gains deductions is volatile, having fluctuated from as low as $18 million to as high as $49 million. TRD adds that, during the recession, taxpayers reported lower capital gains. Because the five-year average used by TRD includes recession years, it may be driven down by lower capital gains deductions from those years.

This FIR therefore provides a range of potential revenue impacts, the upper bound of which uses data from TRD's analysis of similar legislation last year. In 2014, TRD used New Mexico personal income data from tax year 2012 to determine approximately 73,500 people claimed net capital gain deductions totaling $1,190 million. The future years' capital gains deductions were calculated by applying February consensus PIT growth rates to the tax year 2012 estimate, and applying a 4 percent average tax rate to the projected capital gains that would no longer be deductible.

SIGNIFICANT ISSUES

After the 50 percent deduction, capital gains are taxed under the provisions of the Income Tax Act in New Mexico. The following table, from the Tax Foundation, shows how capital gains are taxed at the federal level as of January 1, 2013:

January 1, 2013 -								
If	*and*	Seller's Marginal Income Tax Rate the Year of Sale Is						
Seller Had Owned the Asset for		10%	15%	25%	28%	33%	35%	39.6%
	then	the Tax Rate on the Capital Gain Is						
Less Than 1 Year		10% (a)	15% (a)	25% (a)	28% (a)	33% (a)	38.8%	43.4%
1 Year or More		0% (a)	0% (a)	15% (a)	15% (a)	15% (a)	18.8%	23.8%

Note: The rate remains 28 percent for long-term gains from sales of art works and other collectibles.

(a) The Patient Protection and Affordable Care Act, starting in 2013, imposes an additional 3.8 percent surtax on the lesser of :
-net investment income,
-the excess of the taxpayer's modified AGI over $200,000 (single filers) or $250,000 (joint filers.)
This threshold is based on adjusted gross income, rather than, as with the above rates, taxable income, so it's conceivable that taxpayers in the lower marginal tax brackets could still be subject to the surtax if their AGI is over the threshold but they have lots of itemized deductions. If a taxpayer is in the 35 percent or 39.6 percent bracket, he or she will be definitely subject to the surtax, so it is included in the rate shown for those brackets.

Does the bill meet the Legislative Finance Committee tax policy principles?

1. **Adequacy**: Revenue should be adequate to fund needed government services.
2. **Efficiency**: Tax base should be as broad as possible and avoid excess reliance on one tax.
3. **Equity**: Different taxpayers should be treated fairly.
4. **Simplicity**: Collection should be simple and easily understood.
5. **Accountability**: Preferences should be easy to monitor and evaluate

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