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

SPONSOR Maestas **ORIGINAL DATE** 2/21/17 **LAST UPDATED** 2/23/17 **HB** 503

SHORT TITLE Change Income Tax Bracket and Rates **SB**

ANALYST Graeser

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY17	FY18	FY19	FY20	FY21		
$0.0	($82,400.0)	($209,600)	($214,000.0)	($221,900)	Recurring	General Fund

Parenthesis ( ) indicate expenditure decreases. ** R = recurring; NR = non-recurring

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY17	FY18	FY19	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
Total	Minimal	Minimal	Minimal	Minimal	Recurring	TRD operating

Parenthesis ( ) indicate expenditure decreases. ** R = recurring; NR = non-recurring

Duplicates, Relates to, Conflicts with, Companion to other bills affecting personal income tax rates, including: HB-117, HB-169, HB-201, H-310HB-311 and SB-50. See full list at “CONFLICTS”

SOURCES OF INFORMATION
LFC Files

Responses Received From
Taxation and Revenue Department (TRD)

SUMMARY

Synopsis of Bill

House Bill 503 revises all the lower rates and brackets in the tax tables at 7-2-7 NMSA 1978 and adds a new top bracket with a 6% marginal tax rate in each filing status for personal income tax.

The PIT rate change is applicable to tax years beginning January 1, 2018.

The new scheme, with the higher 6.0 percent rate is as follows:

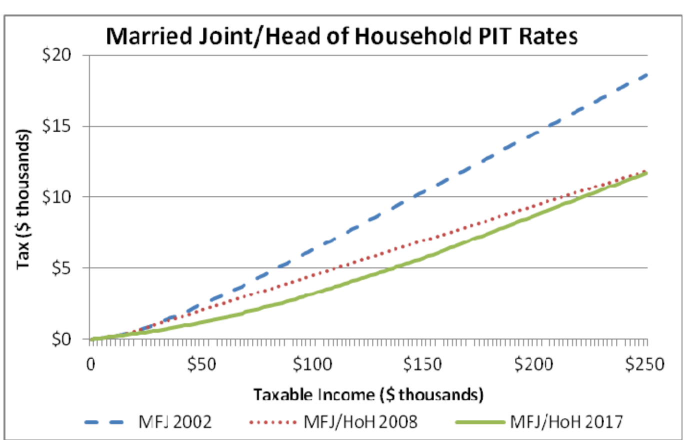
Married Filing Joint, Surviving Spouse, Head of Household				
Taxable Income				
Over	but not over	Tax is	Plus	of amount over
$0	$30,000	0	2.00%	$0
$30,000	$60,000	$600.00	3.00%	$30,000
$60,000	$90,000	$1,500.00	4.00%	$60,000
$90,000	$150,000	$2,700.00	5.00%	$90,000
$150,000	& above	$5,700.00	6.00%	$150,000

Single				
Taxable Income				
over	but not over	Tax is	Plus	of amount over
$0	$20,000	0	2.00%	$0
$20,000	$40,000	$400.00	3.00%	$20,000
$40,000	$60,000	$1,000.00	4.00%	$40,000
$60,000	$100,000	$1,800.00	5.00%	$60,000
$100,000	& above	$3,800.00	6.00%	$100,000

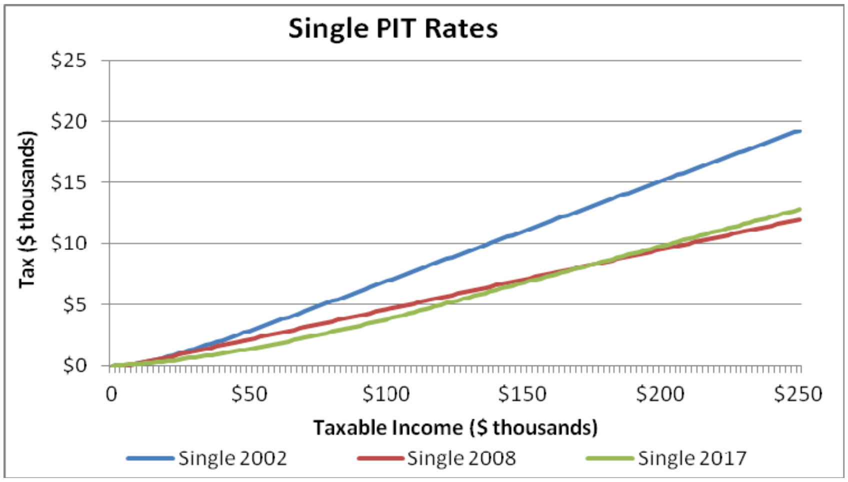
Married Filing Separate				
Taxable Income				
over	but not over	Tax is	Plus	of amount over
$0	$15,000	0	2.00%	$0
$15,000	$30,000	$300.00	3.00%	$15,000
$30,000	$45,000	$750.00	4.00%	$30,000
$45,000	$75,000	$1,350.00	5.00%	$45,000
$75,000	& above	$2,850.00	6.00%	$75,000

FISCAL IMPLICATIONS

This proposal is quite dissimilar to that of HB-310 or any other bill of this session. The provisions of this bill reduce taxes for married joint taxpayers and heads of household (HOH/MFJ) for all taxable incomes up to $250,000 and for single taxpayers (SING) with incomes up to $175,000. The top marginal rate is increased to 5% for MFJ/HoH in excess of $90,000 of taxable income and to 6% in excess of $150,000.



Note that the changes of this bill result in a tax decrease for taxpayers with taxable incomes below about $250,000. Above that cutoff, taxpayers should pay additional amounts over current burden. Also note that this proposal does not restore rates to the 2002 levels.



The detailed tables from TRD are not available. LFC built a rough allocation model that shows the following results:

	HB-503		Current		Difference ($ thousands)
	Average Tax per TP	Total ($1,000)		Average Tax per TP	Total ($1,000)
HOH 0 - 8K	$72	$2,002	$61	$1,702	$300
HOH 8K - 16K	$216	$5,662	$226	$5,914	-$252
HOH 16K-30K	$414	$17,403	$613	$25,765	-$8,361
HOH 30 -60K	$915	$64,691	$1,577	$111,459	-$46,768
HOH 60-90K	$1,800	$85,590	$2,900	$137,871	-$52,281
HOH 90-150K	$3,600	$138,132	$4,884	$187,399	-$49,267
HOH 150K-250K	$7,500	$118,208	$8,412	$132,582	-$14,374
HOH >150K	$61,500	$307,500	$5,2512	$262,560	$44,940
		$739,188		$865,251	-$126,063

	HB-503		Current		Difference ($ thousands)
	Average Tax per TP	Total ($1,000)		Average Tax per TP	Total ($1,000)
SING <5.5K	$50	$1,773	$42	$1,507	$266
SING 5.5K-11K	$149	$4,934	$155	$5,153	-$219
SING 11K-16K	$243	$6,794	$324	$9,046	-$2,252
SING 16K-20K	$324	$6,748	$514	$10,712	-$3,964
SING 20-40K	$610	$36,269	$1,044	$62,044	-$25,775
SING 40-60K	$1,200	$35,486	$1,926	$56,941	-$21,454
SING 60-100K	$2,400	$47,038	$3,249	$63,667	-$16,630
SING 100K-175K	$5,225	$28,738	$5,784	$31,813	-$3,076
SING >175K	$57,800	$149,182	$48,721	$125,748	$23,434
		$315,189		$365,125	-$49,936

This rough model forecasts less revenue reduction in aggregate, but the methodology is crude compared to the TRD methods.

It is useful to note that the very lowest bracket taxpayers will experience a slight tax increase, since the proposed lowest marginal rate is 2% -- up from the current 1.7%. However, this will average less than an additional $10 per taxpayer for the approximately 28,000 in the lowest HOH/MFJ bracket and 36,000 Single filers. Only HOH/MFJ taxpayers with taxable incomes over $250,000 and SING taxpayers with taxable incomes over $175,000 will experience a tax increase.

LFC has adjusted TRD estimates for FY 18, FY 19, FY 20 and FY 21 to decrease the revenue expected to be received in FY 18. The provisions of this bill are effective for tax years beginning January 1, 2018. TRD can adjust withholding tables in its semi-annual update for businesses. A substantial proportion of the taxpayers in the highest bracket – the ones experiencing a tax increase -- will not increase their estimated tax payments. Most personal income taxpayers obliged to pay estimated tax will take advantage of the safe harbor provisions. In the case of the new top bracket (6.0% for MFJ with taxable income over $150,000), the withholding tables would be adjusted for January 2018. Thus, the state would receive the full amount of revenue from higher-income wage and salaried taxpayers beginning with FY 18. However, non-salaried or employed higher-income taxpayers affected by the new rate would probably not adjust their estimated payments and pay off the additional liability as a final settlement in April 2019. These estimates are similar to those calculated by TRD, with the exception that LFC expects 50% of the 80% of the total liability to be paid by withholding to be paid in FY 18.

SIGNIFICANT ISSUES

LFC staff note that this bill clearly proposes a tax increase for higher-income taxpayers. On the other hand, it can be seen as partially restoring a previous (2003) PIT rate cut. The 2003 cut was enacted in an attempt to make the state more attractive to businesses seeking to relocate or expand. The current state of the economy essentially proves that many, if not all, of the tax changes enacted since 2003 have not been effective in stimulating job growth and economic opportunities.

A tax expenditure occurs when a particular deduction or exemption (reducing revenue) is used to define a tax base that is normative compared to similar provisions in other states (or countries). Whether a personal income tax should be progressive, neutral or regressive is an interesting discussion of this principle. In history, New Mexico's personal income tax, with a succession of universal and low-income food and medical tax rebates served as a balance wheel. The progressive PIT rate structure balanced the moderately regressive gross receipts tax (which has become far more regressive as we enact tax expenditures relieving higher-income taxpayers of tax liability) and the proportional to regressive property tax. The income elasticity of the current tax is about 1.0, meaning that a 10 percent increase in personal income results in a 10 percent increase in personal income tax. Prior to the 2003 Governor Richardson era PIT rate reduction, the income elasticity was between 1.3 and 1.4, meaning that a 10 percent increase in personal income resulted in a 13 to 14 percent increase in personal income tax. Rearranging the lower brackets and establishing the higher income top bracket will likely increase the income elasticity of the tax to about 1.3. This would help balance the budgets in future years. This possible effect has not been included in the fiscal impact reported in the summary table.

ADMINISTRATIVE IMPLICATIONS

Minimal

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP: relates to all other bills amending the personal income tax act. These include at this point: HB 48, HB 61, HB 68, HB 82, HB 117, HB 169, HB 193, HB 201, HB 222, HB 310, HB 311, HB 324, HB 365, HB 376, HB 503, HB 504, SB 41, SB 50, SB 123, SB 196, SB 274, SB 326, SB 343

TECHNICAL ISSUES

Other versions of this bill adjusting the PIT rates have contained a repealer of 2005 (1^{st} SS) version of 7-2-7 NMSA 1978, the bill that adjusted the timing of the phase-down in PIT rates. These changes have now been in place more than three years plus the current year and returns from those years are not eligible for amendment. This repeal will modestly clean up current statute.

LG/sb/jle/al/jle