FISCAL IMPACT REPORT

SPONSOR	Reps. Cortez, Murphy, Block, and Montoya/Sen. Block	**LAST UPDATED**	2/11/25
		ORIGINAL DATE	2/10/2025
SHORT TITLE	Eliminate Personal Income Tax	**BILL NUMBER**	House Bill 275
		ANALYST	Gray/Torres

REVENUE*
(dollars in thousands)

Type	FY25	FY26	FY27	FY28	FY29	Recurring or Nonrecurring	Fund Affected
Personal Income Tax & Corporate Income Tax	$0	($1,800,000)	($3,800,000)	($3,900,000)	($4,100,000)	Recurring	General Fund

Parentheses ( ) indicate revenue decreases.
*Amounts reflect most recent analysis of this legislation.

Because of the short timeframe between the introduction of this bill and its first hearing, LFC has yet to receive analysis from state, education, or judicial agencies. This analysis could be updated if that analysis is received.

SUMMARY

Synopsis of House Bill 275

House Bill 275 (HB275) sets the personal income tax rate equal to zero percent beginning in tax year 2026. The bill also provides that filing personal income tax returns is not required but may still be filed.

FISCAL IMPLICATIONS

The bill is estimated to reduce recurring general fund revenues by $1.8 billion in FY26 and by $3.8 billion in FY27. This impact was estimated using the December 2024 Consensus Revenue Estimating Group (CREG) personal income tax forecast for personal income tax withholding, estimated payments and final settlements, oil and gas proceeds withholding, pass-through entity withholding, and fiduciary payments. The bill does not contemplate changes to personal income tax credits, deductions, or exemptions. The cost of those tax programs will likely increase; this analysis assumes they remain flat with current estimates, meaning the true cost of the legislation may be higher than what is presented in this analysis.

The income tax covers a broad array of taxpayers, including wage earners, some businesses filing as pass-through entities, individuals who own stakes in oil and gas extraction, and estates and trusts. These taxpayers would also have an income tax rate of zero. In FY24, the size of each personal income tax program was as follows:

FY24 PIT Revenue Estimate by Component (in millions)	
PIT Program	Revenue
Wage Withholding	$2,132.1
Est. Payments / Final Settlements	$661.3
OGAS Withholding	$243.1
Pass-Thru Withholding	$105.1
Fiduciary	$35.5
	Source: December 2024 CREG

The estimates by the Consensus Revenue Estimating Group (CREG) for these programs in future years was used for the costs illustrated on page 1. The estimates assume equal refunds, credits, and rebates to taxpayers from current law. Estimates also assume the refunds currently issued remain under this bill. To the extent credits are nonrefundable and refunds are reduced from taxpayers withholding amounts in excess of their tax liability, the costs estimated may be smaller than represented here. However, those risks are offset by the possibility refunds grow due to larger rebates and credits, which will inflate with an eliminated tax liability and a new incentive to file taxes, especially for lower income individuals, with a high likelihood for refund and no chance for tax liability.

The following table shows modeled tax savings and share of taxpayers by tax bracket.

HB275 Average Tax Savings by Income Bracket

Brackets	Taxable Income Range	Old Rate	Brackets	Taxable Income Range	New Rate	Average Tax Savings*	Share of Filers
Married Filing Jointly, Heads of Households							
1	$0 - $8,000	1.5%	1	$0 - $8,000	0.0%	$0	39%
2	$8,000 - $25,000	3.2%	2	$8,000 - $25,000	0.0%	$289	11%
3	$25,000 - $50,000	4.3%	3	$25,000 - $50,000	0.0%	$1,109	15%
4	$50,000 - $100,000	4.7%	4	$50,000 - $100,000	0.0%	$2,603	17%
5	$100,000 - $315,000	4.9%	5	$100,000 - $315,000	0.0%	$6,602	16%
6	$315,000 -	5.9%	6	$315,000 -	0.0%	$29,528	2%
Single							
1	$0 - $5,500	1.5%	1	$0 - $5,500	0.0%	$0	44%
2	$5,500 - $16,500	3.2%	2	$5,500 - $16,500	0.0%	$152	12%
3	$16,500 - $33,500	4.3%	3	$16,500 - $33,500	0.0%	$718	20%
4	$33,500 - $66,500	4.7%	4	$33,500 - $66,500	0.0%	$1,727	14%
5	$66,500 - $210,000	4.9%	5	$66,500 - $210,000	0.0%	$4,088	9%
6	$210,000 -	5.9%	6	$210,000 -	0.0%	$22,199	1%

*Note that for taxpayers with taxable incomes from $0 to $8,000 tax savings may be higher but are not included in this analysis.

Source: LFC Analysis

SIGNIFICANT ISSUES

Most U.S. states levy individual income taxes, with 41 taxing wage and salary income, while seven states impose no income tax. Among those that tax wages, 12 use a flat tax structure, applying a single rate to all taxable income, while 29 states and the District of Columbia use a graduated system with varying brackets. Hawaii has the most brackets, with 12 tax brackets. See *Attachment 1* for a map of states ranked only by the highest top marginal income tax rate, which does not represent effective personal income tax rates, which was 2.1 percent in New Mexico in tax year 2023.

Personal income tax represented about 17 percent of recurring general fund revenues in FY24. The personal income tax is an important tax policy tool used to further both horizontal equity, by ensuring the same statutes apply to all taxpayers, and vertical equity, by ensuring the tax burden is based on a taxpayers' ability to pay.

In assessing all tax legislation, LFC staff considers whether the proposal is aligned with committee-adopted tax policy principles. Those five principles:

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

The bill contemplates a major tax policy change and will have wide-ranging economic implications.

The elimination of personal income tax is expected to benefit taxpayers by increasing disposable income, potentially leading to higher consumer spending and economic growth as some businesses experience an increase in activity. Eliminating income taxes could improve the state's business climate, making New Mexico more attractive to businesses and residents compared to neighboring states with currently lower tax burdens. Additionally, removing the income tax could simplify tax compliance, reducing administrative burdens on both taxpayers and the Taxation and Revenue Department.

Several states across the country are making significant changes to their individual income tax structures, continuing a trend since the pandemic in some states of tax reduction. On January 1, 2025, nine states—Indiana, Iowa, Louisiana, Mississippi, Missouri, Nebraska, New Mexico, North Carolina, and West Virginia—will reduce individual income tax rates, with South Carolina making a previously temporary rate reduction permanent. These reductions come as part of ongoing efforts to improve tax competitiveness, stimulate economic growth, and provide relief to taxpayers.

Among these changes, Iowa and Louisiana are in the process of transitioning to single-rate income tax systems, while New Hampshire, which previously taxed interest and dividends, has repealed this tax entirely, completing its transition to a state without personal income tax. Hawaii, a state that historically has not automatically adjusted its tax brackets for inflation, will implement significantly wider tax brackets in 2025. This adjustment will expose more income to lower marginal tax rates, reducing the tax burden on all taxpayers.

New Mexico has participated in these trends by reducing total income taxes by an estimated $811 million, by FY28, due to tax changes made over the last five years. These reductions include the most recent expansion of lower income brackets to provide tax relief targeted at low-income individuals but benefiting all taxpayers.

Concurrently, this analysis notes eliminating the personal income tax will reduce government spending, which may have a negative impact on economic activity and other forms of state revenues, like that from the gross receipts tax (GRT). Businesses that benefit from spending may see a decrease in activity as state government necessarily decreases spending that would have otherwise occurred, which may translate into decreased job creation. The magnitude and interaction of these impacts and positive impacts from expanded consumer spending are offsetting and not studied in detail in this report.

The elimination of the personal income tax also creates substantial fiscal challenges. Personal income tax is one of the largest sources of revenue for the state general fund, contributing to essential services, such as education, healthcare, and public safety. Without this revenue, the state would lower spending or increase the GRT and other taxes or find alternative revenue sources to maintain current service levels. Severance taxes allow the state to reduce the overall tax burden as an alternative revenue source, but severance taxes are volatile and are estimated to decline in the long run. Increasing reliance on these sources increases revenue volatility, challenges strategic fiscal planning, and shifts tax burdens significantly.

Another potential consequence of eliminating the tax is the effect on the state's ability to respond to economic downturns. Personal income tax revenue provides the most stable source of general funds, according to the most recent LFC Revenue Volatility Analysis.[1] This is particularly important during recessions or energy market declines when other revenue streams, such as gross receipts tax and oil and gas revenues, decline severely. Without income tax revenue, the state would become more dependent on volatile sources, increasing the risk of budget shortfalls and budget cuts during economic downturns.

The proposal could also impact New Mexico's bond ratings and the state's ability to finance capital projects. New Mexico relies on a stable revenue base to secure favorable credit ratings for bonds used to fund infrastructure, schools, and public facilities. Removing personal income tax revenue without a clearly defined replacement strategy could lead to credit downgrades, as was the case for Mississippi among other issues, according to S&P Global.[2] Downgrades increase the cost of borrowing and limit the state's capacity to invest in long-term projects. States that have eliminated or significantly reduced income taxes, such as Kansas, have experienced fiscal instability, leading to cuts in essential services and declining credit ratings.[3]

Furthermore, while taxpayers would no longer be required to file state income tax returns, they would still need to file federal returns, and certain credits and deductions linked to state filings could become unavailable or require adjustments. This could create unintended consequences for individuals who rely on state income tax structures for specific financial planning strategies, such as deductions for retirement savings or business expenses.

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[1] https://www.nmlegis.gov/Handouts/ALFC%20071524%20Item%2012%20Revenue%20Volatility%20Report.pdf
[2] https://disclosure.spglobal.com/ratings/en/regulatory/article/-/view/type/HTML/id/3133438
[3] https://www.reuters.com/article/markets/us/sp-downgrades-kansas-in-another-blow-to-brownback-tax-cuts-idUSL2N0QC1MO/

Equity concerns also arise with this proposal. Eliminating the income tax benefits higher-income earners disproportionately because they currently pay the largest share of state income tax. Lower-income individuals, who already pay little or no income tax, may not see significant benefits but could experience increased tax burdens if the state shifts toward regressive revenue sources, such as the GRT.

HB275 does not align with the LFC tax policy principle of efficiency, in which the tax base should be as broad as possible to avoid excess reliance on one tax. The state is primarily reliant on three primary tax revenue sources: GRT, severance taxes and interest, and income taxes. By removing income from the tax base, the state will necessarily become more reliant on other forms of taxation. This comes with tradeoffs. GRT is New Mexico's least competitive tax because it can translate into tax pyramiding and remains higher than most other states due to high local increments, which may hurt business competitiveness.

Attachment:

Map of Top Marginal State Income Tax Rates

BG/IT/hj/SR/hg/sgs

Attachment 1. Map of Top Marginal State Income Tax Rates.

Source: Tax Foundation