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

SPONSOR: SFC DATE TYPED: 03/16/01 HB

SHORT TITLE: Reduce Income Tax Rates SB 124 et al/SFCS/aSFl #1/ aHTRC/aCC #1/aCC #2

ANALYST: Williams

REVENUE

Estimated Revenue		Subsequent Years Impact	Recurring or Non-Rec	Fund Affected
FY01	FY02			
	$ (31,540.0)	$ (39,180.0)	Recurring	General Fund
	$ (30,600.0)	$ (1,300.0)	Non-recurring	General Fund
	$ (1,790.0)	$ (2,420.0)	Recurring	Local Governments

(Parenthesis ( ) Indicate Revenue Decreases)

SOURCES OF INFORMATION

LFC Files
Taxation and Revenue Department (TRD)

SUMMARY

Significant Issues

TRD notes, unless amended, the expansion of the gross receipts tax medicare deduction probably includes payments to for-profit hospitals unless amended.

Synopsis of Conference Committee Amendments (round two)

The proposal is exactly the same as the first round of conference committee amendments.

Synopsis of Conference Committee Amendments (round one)

The proposal scales back the rebate program to only one year, rather than two. This component is the non-recurring piece of the bill. There are various technical amendments to clarify the Medicare deduction for health care practitioners.

Synopsis of HTRC Amendments

The HTRC amendments strike the Senate floor amendment and virtually all of the text of the bill thus far. The amendments then insert language to authorize the following:

With respect to personal income taxes, the bill reduces the top income tax rates over two years. In tax year 2001, the highest personal income tax rate would decline from the current 8.2% to 7.8%. In tax year 2003, the top rate is reduced to 7.7%. The second highest rate, drops from 7.9% to 7.1%. There are no other rate changes in the package. The second highest income bracket is broadened. The design features also reduce the marriage tax penalty of the state income tax. This component of the bill results in an average tax decrease per return of $53.

The bill authorizes a new, refundable income tax rebate for New Mexico residents for tax year 2001 and 2002. The amount of the rebate ranges from $30 for single, married filing separate to $60 for married, filing joint returns. The rebate is targeted to those taxpayers below certain taxable income levels, ranging from $32,000 for married, filing separate returns to $64,000 married, filing joint.

The bill increases the current low income comprehensive tax rebate (LICTR) effective tax year 2001. Taxpayers would now be able to claim two additional exemptions for each minor child or stepchild for a total of three exemptions for children. In addition, the cell amounts in the LICTR table are increased by an average of 15%.

LICTR benefits would be:

- one adult/1 child: +$135/year
- one adult/2 or more children: +$230/year
- two adults/1 child: +$120/year
- two adults/2 or more children: $260/year

Effective tax year 2001, the pilot job mentorship tax credit becomes a permanent tax credit. The bill would permanently authorize the job mentorship tax credit, a pilot program authorized for tax years 1999 through 2001. The current program sunsets effective January 1, 2002. The bill would eliminate the 1,000 student participant cap on the current program.

The credit could be claimed against personal and corporate income taxes, and its purpose is to encourage businesses to hire youth participating in certified school-to-career programs. The credit is limited to 50% of the gross wages paid to a qualified student participating in a certified school-to-work program. A qualified student is between 14 and 21 years of age. The maximum aggregate credit per business shall not exceed 50% of the gross wages paid to no more than 10 qualified students employed for up 320 hours in a taxable year (only two months if working a 40 hour week). The total credit cannot exceed $12,000 thousand per year and can only be used to offset the tax liability of the taxpayer. Any unused portion may be carried forward for three years. The taxpayer must certify that hiring the qualified student does not displace or replace a current employee. Administrative responsibility rests with the School to Work Office of the Department of Finance and Administration which operates 17 school-to-work regional partnerships.

For gross receipts taxes, the bill authorizes a gross receipts tax deduction for certain shared costs between franchisee and franchiser. The shared costs of developing, maintaining or modifying a reservation system (such as those used by car rental agencies or hotels) would become deductible. Hotels, motels and the like may reimburse the franchiser for payments of commission to travel agents for booking guests without tax imposed on the franchiser. Amounts paid by a franchisee to the franchiser for training are deductible. Finally receipts of an advertising cooperative from franchisee or franchiser are deductible. These deductions are proposed to change the future impact of a series of audits by TRD that resulted in multimillion dollar assessments.

The bill expands the 1998 gross receipts tax deduction for Medicare Part B receipts to all health care practitioners and to home health agencies.

The receipts from payments by a third-party administrator of the federal TRICARE program may also be deducted from gross receipts tax. TRICARE is a managed care health insurance similar to the state's SALUD program for Medicaid recipients, or various managed care private insurance programs. Three types of Tricare are available to active duty military, military retirees and their families. Roughly 3.9% of the state's population is covered by TRICARE.

In Section 4, the bill requires every taxpayer to declare the same filing status and number of personal exemptions as for federal income tax purposes, effective tax year 2001.

Synopsis of Senate Floor Amendment #1

The amendment made a technical clarifying amendment to add the January 1, 2002 effective date to Section 3.

Synopsis of SFC Substitute

This proposal is a two-year tax cut, with about one-half of the impact in the first year.

By the second year, the top rate of 8.2% is reduced by 0.4% to 7.8% to address economic development issues for the state. Other rates drop as well to help give tax relief to all New Mexicans.

A zero bracket component provides a 0% tax rate for married filing joint taxpayers up to $4,400 in income. Just under 50,000 returns would be dropped from having personal income tax liability in the first year, and about 65,000 returns in the second year.

The proposal also includes an expansion of the low income comprehensive tax rebate (LICTR) program. The LICTR program would be amended to increase the number of exemptions allowed for each child in a household by two, thereby treating children in an equal manner as the elderly. The fiscal impact of amending the LICTR program in this manner would be approximately $4.5 million. Approximately 65% of the net benefit will go to families and heads of households with 1 child and the balance to families with 2 or more children.

The design features also reduce the marriage tax penalty of the state income tax.

Synopsis of Original Bill

The bill authorizes a reduction in personal income taxes and is consistent with the proposal endorsed by the Governor.

The bill creates a zero bracket amount which would result in qualifying taxpayers avoiding filing. Zero bracket proposals typically impact lower income tax payers, while reducing general fund revenue on a recurring basis. TRD estimates 65,000 returns would be dropped from liability from this tax package.

Tax rates would then be adjusted as follows: 2.0%, 3.0%, 4.5%, 6.0%, 7.1% and 7.7%, compared to the current: 1.7%, 3.2%, 4.7%, 6.0%, 7.1%, 7.9% and 8.2%. Note that the top rate drops by 0.5%. Rate cut proposals also reduce general fund revenue on a recurring basis.

A proposed bracket change just tracks current law, after updating for the proposed rate changes.

TRD notes the proposal is designed to try to reduce marriage tax penalty impacts. The bill is applicable beginning tax year 2001.

FISCAL IMPLICATIONS

Synopsis of Conference Committee amendments

The significant fiscal impact changes from these amendments is reduction of the non-recurring rebate to only one year. TRD indicates the non-recurring general fund revenue loss is $30,600.0 in FY02 and $1,300.0 in FY03. The recurring components of the bill are projected to reduce general fund revenues by $31,540.0 in FY02 and $39,180.0 in FY03. The total general fund revenue loss from the tax package in its current form is projected by TRD at $62,140.0 in FY02 and $40,480.0 in FY03. In addition, the proposal would reduce local government revenues by $1,790.0 in FY02 and $2,420.0 in FY03.

Synopsis of HTRC Amendments

General fund revenue loss in FY 02 is broken into two components: a $31,600.0 recurring general fund revenue loss and what is intended to be a non-recurring reduction of $30,500.0. The total amount in the first year of the general fund revenue reduction is $62,100.0.

The FY03 general fund revenue loss is projected at a recurring $40,500.0 and a non-recurring revenue loss of $32,500.0. The total amount of revenue reduction in the second year is $73,000.0.

The overall reductions of the personal income tax rate and brackets changes with tax relief by group, share of taxpayers in each group and each group's share of tax relief are summarized in the attached tables.

Local governments are impacted by the franchisee gross receipts, Medicare B gross receipts and TRICARE gross receipts deduction expansions. The total recurring local government revenue loss is projected at $1,600.0 in FY02 and $1,600.0 in FY03.

The Taxation and Revenue Department has not submitted a fiscal impact analysis on the last version of this bill.

Synopsis of SFC Substitute

Total net general fund cost for the first year of this personal income tax package is estimated to be $35.2 million in FY02 and $71.9 million in FY03.

The LICTR component results in an average increase of $20 per LICTR family.

The first year proposal of tax reduction results in an average decrease per return of $55, with every category of income receiving a tax reduction. The average tax cut per return rises to $122 in the second year.

Synopsis of Original Bill

TRD has estimated that the proposed changes would decrease general fund revenues by $72,500.0 million in FY02 and by $72.1 million in FY03. TRD's estimate of the distribution of tax relief by income class is shown on the attached table.

ADMINISTRATIVE IMPLICATIONS

TRD reports that it can absorb most of the proposed changes within existing resources. However, the franchisors change will require considerable effort to determine how to unbundle the franchise payment to a royalty portion, advertising, reservation system and other components.

AW/jsp:ar
Attachments