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

| | | | | | |
|---|---|---|---|---|---|
| | | **ORIGINAL DATE** | 2/15/17 | | |
| **SPONSOR** | Maestas | **LAST UPDATED** | | **HB** | 324 |
| **SHORT TITLE** | Additional Tax Brackets | | | **SB** | |
| | | | | **ANALYST** | Graeser |

## REVENUE (dollars in thousands)

| Estimated Revenue | | | | | Recurring or Nonrecurring | Fund Affected |
|---|---|---|---|---|---|---|
| **FY17** | **FY18** | **FY19** | **FY20** | **FY21** | | |
| 0.0 | 21,750.0 | 44,400.0 | 45,900.0 | 47,400.0 | Recurring | General Fund |

Parenthesis ( ) indicate expenditure decreases.

Duplicates, Relates to, Conflicts with, Companion to: See comprehensive list later in this bill review.

**SOURCES OF INFORMATION**
LFC Files

Responses Received From
Taxation and Revenue Department (TRD)

**SUMMARY**

Synopsis

House Bill 324 adds an additional tax bracket for married individuals filing separately (SEP) with income over $109,091 of $5,141.46 plus 5.9% of the excess over $109,091; $10,282.92 plus 5.9% of excess over $218,182 for heads of household (HOH), surviving spouses and married individuals filing jointly; and $7,070.50 plus 5.9% of excess over $150,000 for single individuals (SNGL) and for estates and trusts with income over $150,000.

Effective date is not specified; 90 days following adjournment (June 16, 2017);
Applicability: the provisions of this act apply to taxable years beginning on or after January 1, 2018.

**FISCAL IMPLICATIONS**

This bill partially reverses the Richardson-era PIT rate cuts.

TRD prepared the following estimate and commentary:

> The Taxation and Revenue Department (TRD) used GenTax taxpayer data from tax years 2010-2015 to estimate the revenue impact. Tax year 2014 is considered the most current dataset for this analysis. PIT growth rates forecast by the Consensus Revenue Estimating Group (CREG) December 2016 were used to estimate out-year revenues. This estimate assumes that existing taxpayers who are impacted by this bill will remain in the state. A detailed discussion of methodology is provided below.

| Estimated Revenue Impact* | | | | | R or NR** | Fund(s) Affected |
|---|---|---|---|---|---|---|
| FY2017 | FY2018 | FY2019 | FY2020 | FY2021 | | |
| $- | $- | $21,750 | $44,400 | $45,900 | R | General Fund |

The timing of revenues from this bill will be somewhat different than indicated by TRD. The added bracket will be effective for tax years beginning January 1, 2018. TRD will be able to adjust the withholding tables effective January 1, 2018. Thus, in FY 18, TRD will receive ½ year's withholding revenue. Taxpayers who file estimated tax payments will likely take advantage of the "safe harbor" rule and not increase estimated payments. Therefore, the amounts reported by TRD are acceptable, but the timing will be advanced by one full fiscal year than shown. This change is shown in the main revenue table on page 1 of this review.

All of the bills in this legislative session that propose restoring a top marginal PIT bracket will generate revenue (i.e., a tax increase). However, these bills will also change the personal income tax from largely proportional and non-buoyant, with an income elasticity of 1.0 to a progressive tax with an income elasticity of between 1.15 to 1.20. That is, under current law, a 10% increase in state personal income will increase personal income tax liabilities by 10%. With the top bracket restored, the same 10% increase in personal income will result in an increase of 15% to 20% in PIT liabilities.

## SIGNIFICANT ISSUES

TRD notes, "… this legislation implicates the tax policy principal of vertical equity by increasing the tax rate on certain taxpayers. Based on tax year 2014 data, approximately 64% of all personal income tax (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 income multiplier of this legislation (1.0, 2.0, & 1.38) deviates from the statutory multiples for lower thresholds (1.0, 2.0, 1.5). Horizontal equity ensures similarly-situated taxpayers face similar tax burdens. To align the new brackets to the existing multiple schedule, the new thresholds would be $109,091, $218,182, and $163,637 for SEP, HOH, and SNGL respectively. (Or, alternatively, $100K, $200K, and $150K for SEP, HOH, and SNGL respectively).

## PERFORMANCE IMPLICATIONS

The LFC tax policy of accountability is effectively met with TRD's commitment to publish annually the Tax Expenditure Report. Although this report focuses primarily on general fund costs of various tax expenditures, each edition of the report extends the analysis of goals and economic consequences of any particular tax expenditure. The revenues above baseline of this change are estimated above. These estimates of total revenue will be compared annually by the consensus revenue estimating group in the quarterly updates of revenue performance.

**ADMINISTRATIVE IMPLICATIONS**

TRD reports minimal administrative impact -- costs for updating systems and forms can be absorbed in annual tax year updates.

| Estimated Additional Operating Budget Impact* | | | | R or NR** | Fund(s) or Agency Affected |
|---|---|---|---|---|---|
| FY2017 | FY2018 | FY2019 | FY 17-19 | | |
| | $25 | 0 | $25 | NR | Taxation and Revenue Department |

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

**CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP**

Bills in the 2017 Session that amend portions of the personal income tax provisions:

| Bill ID | Title |
|---|---|
| HB 48 | SMALL BUSINESS INCOME TAX DEDUCTION |
| HB 61 | EXTEND SOLAR MARKET TAX CREDIT |
| HB 68 | RURAL HEALTH CARE PRACTITIONER TAX CREDIT |
| HB 82 | EXTEND SOLAR MARKET TAX CREDIT |
| HB 117 | SUPPLEMENTAL INCOME TAX |
| HB 169 | INCOME TAX DEDUCTIONS |
| HB 193 | SOLAR MARKET TAX CREDIT PERMANENT |
| HB 201 | NEW TOP INCOME TAX BRACKET |
| HB 222 | SPECIAL NEEDS ADOPTED CHILD TAX CREDIT AMOUNT |
| HB 310 | INCOME & CAPITAL GAINS TAXES |
| HB 311 | INCREASE WORKING FAMILIES TAX CREDIT |
| HB 324 | ADDITIONAL TAX BRACKETS |
| HB 365 | LIMIT CAPITAL GAINS DEDUCTION |
| SB 41 | EXTEND SOLAR MARKET TAX CREDIT |
| SB 50 | ADDITIONAL UPPER-TIER TAX BRACKETS |
| SB 123 | TAX REFORM |
| SB 196 | SMALL BUSINESS INVESTMENT TAX CREDIT |
| SB 274 | TAX DETERMINATION OF IN-STATE SALE & SERVICES |
| SB 326 | FRONTIER COMMUNITY INVESTMENT TAX CREDITS |
| SB 343 | CHANGES TO TAX CODE PROVISIONS |

## OTHER SUBSTANTIVE ISSUES

TRD explains its revenue estimating methodology:

> … TRD used GenTax taxpayer data to estimate the revenue impact. Tax year 2014 is considered the most current dataset for this analysis. PIT growth rates forecast by the CREG December 2016 were used to estimate out-year revenues.
>
> Line 17 of PIT-1 was used to identify qualifying taxpayers. The new revenue estimate attributed to the tax increase was calculated by applying the proposed tax rate to the difference between total taxable NM income and the income bracket floor for each filing status. Total taxable NM income was derived from line 11, column 2 of the PIT-B form if a PIT-B was filed and line 18a of PIT-1 reflected 'B', or line 17 of PIT-1 if line 18a reflected 'R'. "B" indicates the taxpayer filed a PIT-B; "R" indicates the taxpayer did not file a PIT-B and used the published rate tables.
>
> Estimates from tax years 2013 & 2014 were used to forecast the revenue gain. In general, CREG estimates that 60% of fiscal year PIT collections are for the prior tax year, and 40% are from preceding tax years (i.e. FY2015 PIT is the sum of 60% of tax year 2014 liabilities and 40% of tax year 2013 liabilities). The PIT growth rates from the December 2016 CREG forecast were applied to the new revenue estimate.

LG/jle