State Personal Income Taxation: Issues and Developments

Presented to the New Mexico Revenue Stabilization and Tax Policy Committee

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About ITEP

The Institute on Taxation and Economic Policy (ITEP)

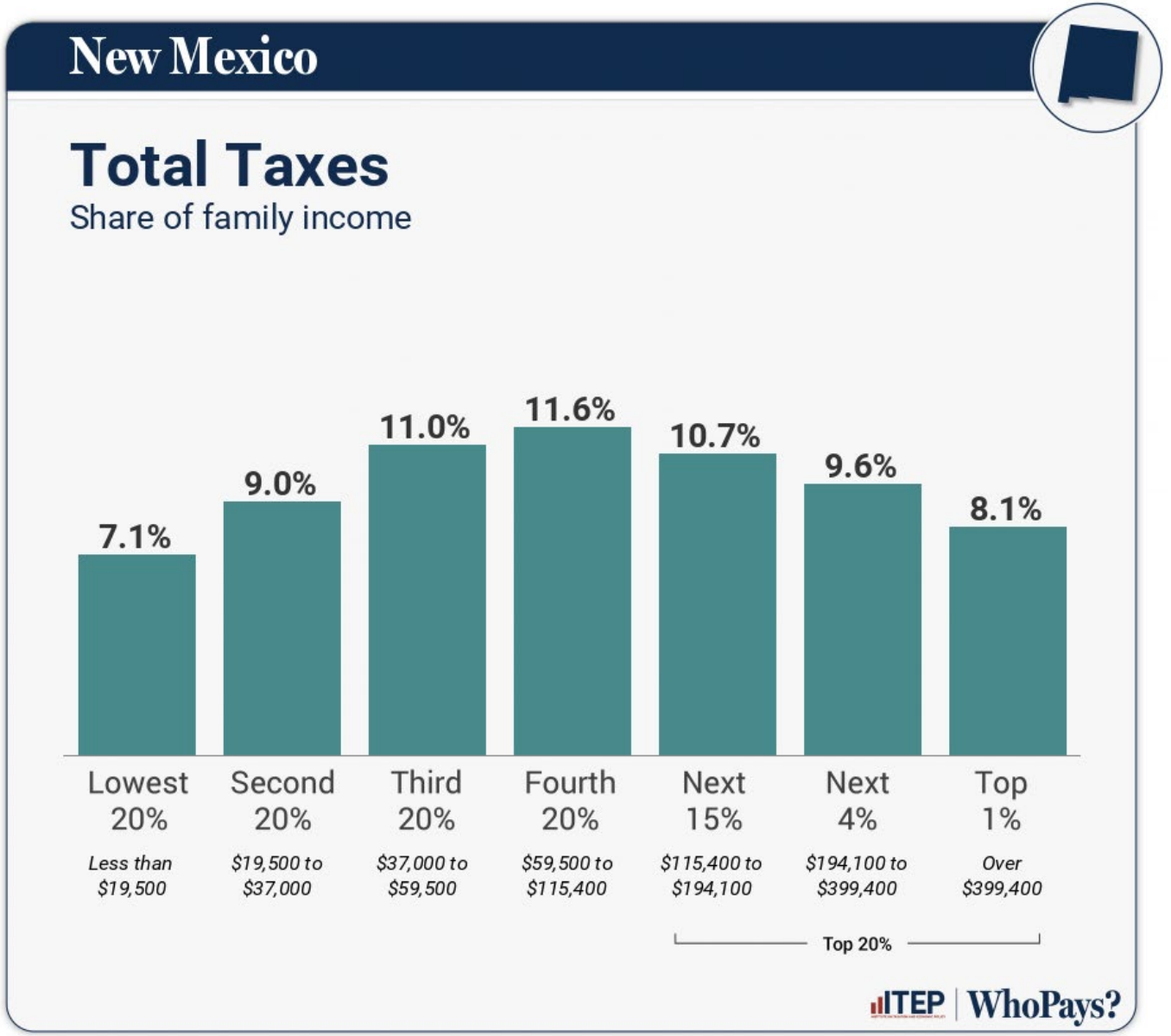
- Non-profit, non-partisan
- Federal, state, and local tax policy issues
- Focus on data and research



4 Topics for Today

1. Competing ideas for working-class tax cuts.
2. Tax cuts/increases for people with high income or wealth.
3. How new federal tax laws affect NM's personal income tax.
4. Tax enforcement.

A Distributional Analysis of Who Pays New Mexico Taxes

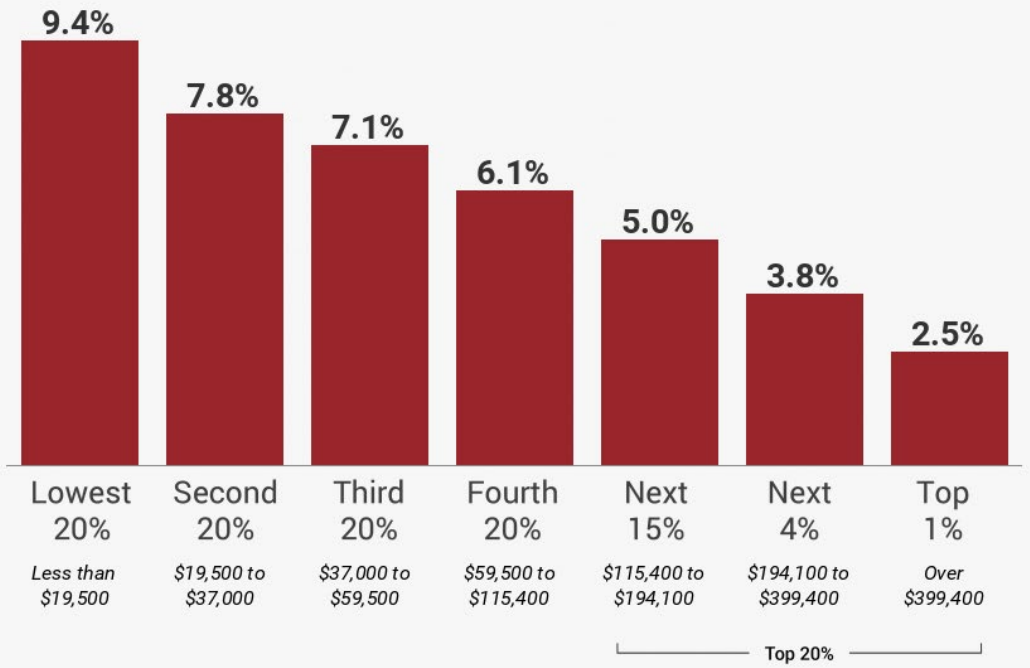


Source: Institute on Taxation and Economic Policy, January 2024.

New Mexico

Sales & Excise Taxes

Share of family income

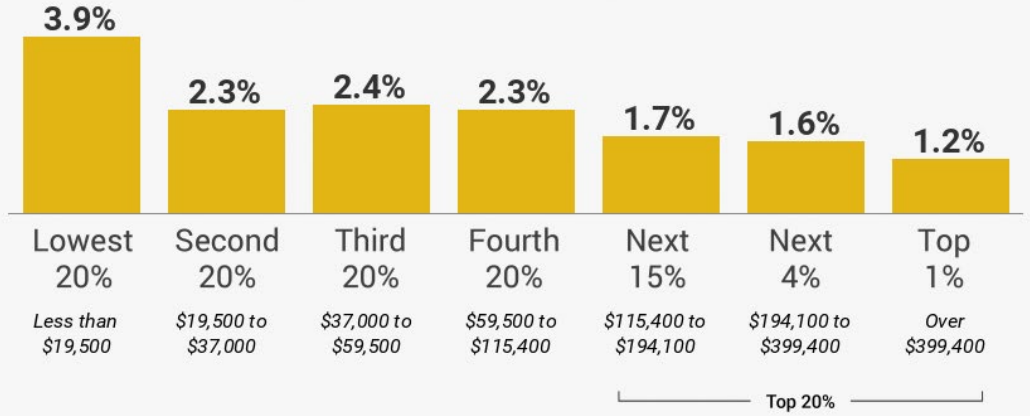


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New Mexico

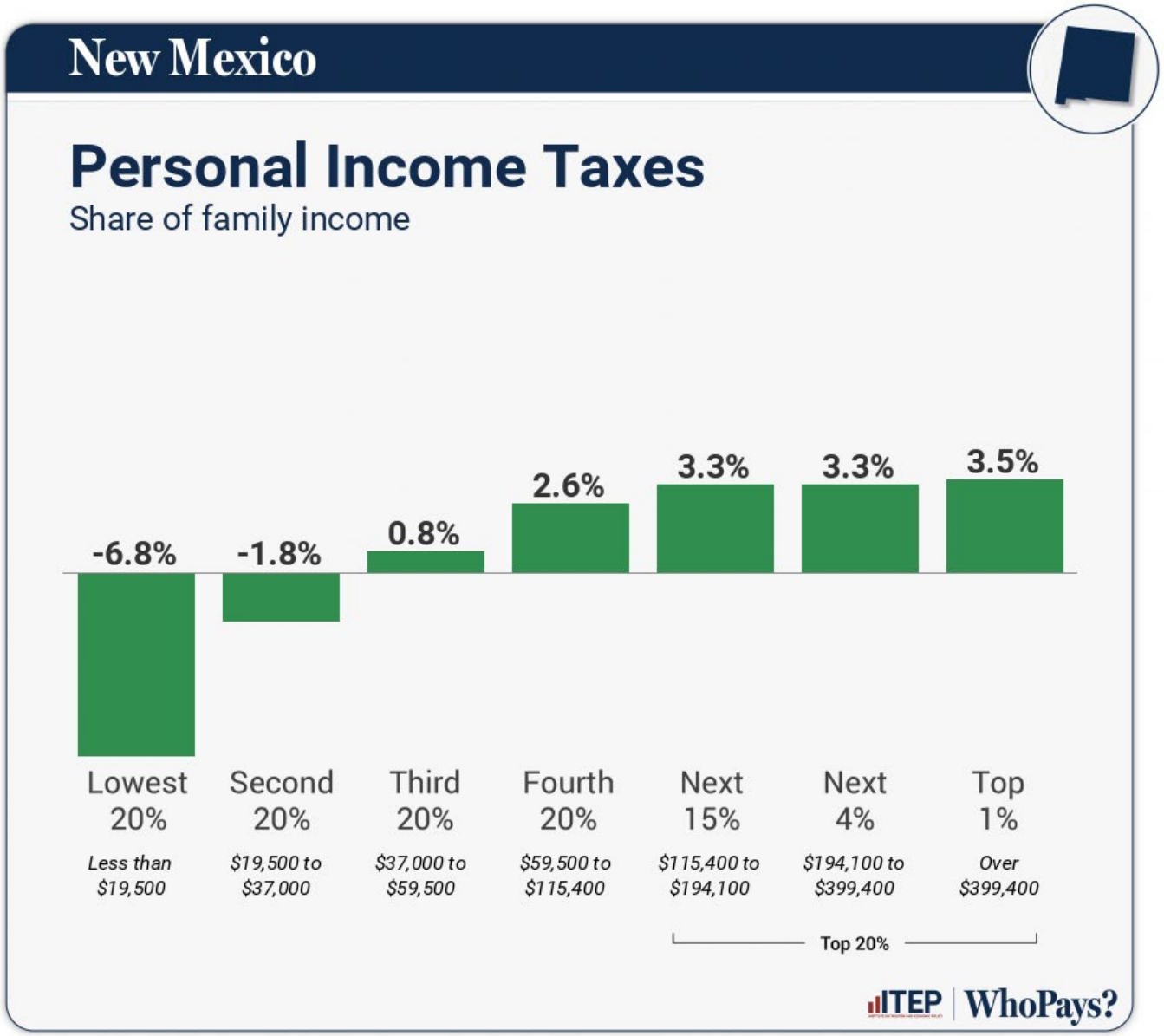
Property Taxes

Share of family income



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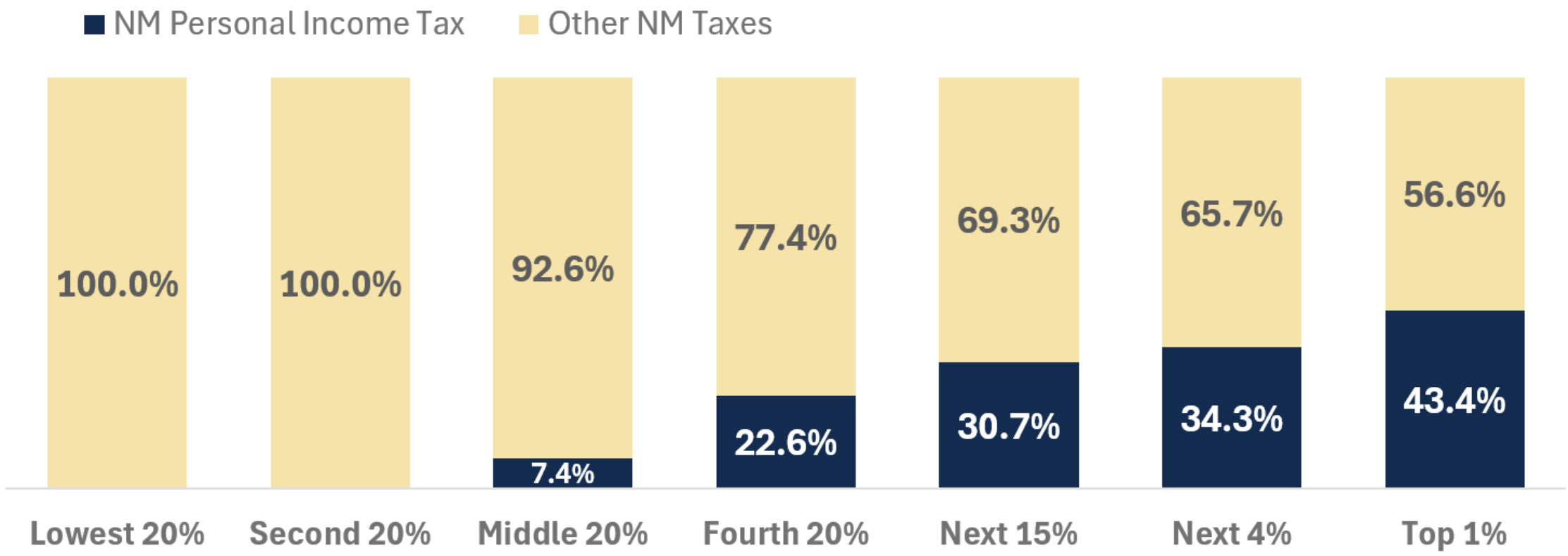
New Mexico Personal Income Provides Some Balance Against Otherwise Regressive Taxes (GRT, excise, property, etc.)



Source: Institute on Taxation and Economic Policy, January 2024.

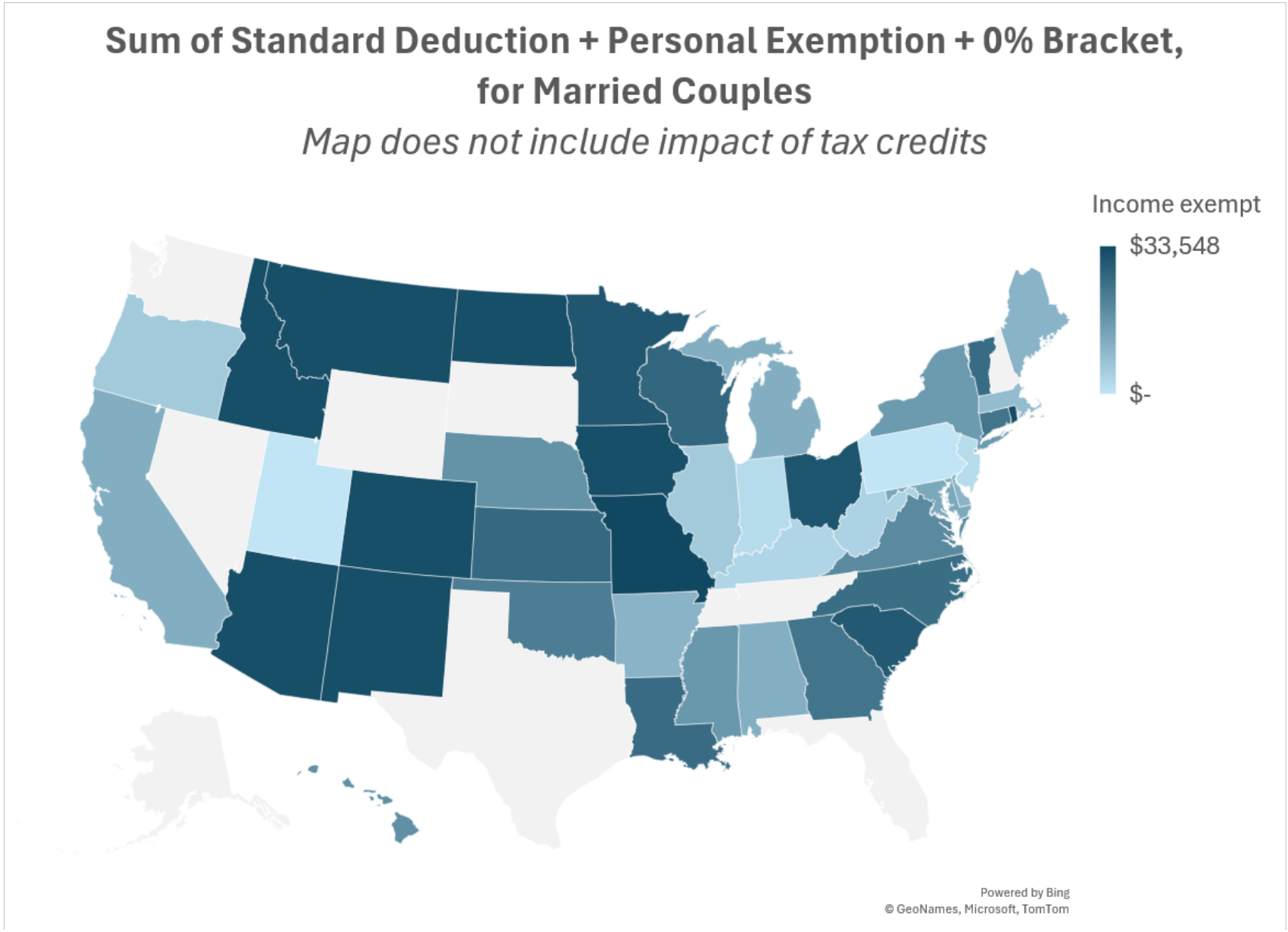
Most Tax Paid by New Mexicans is Not Personal Income Tax

Personal income tax paid as a percent of NM tax, by income group

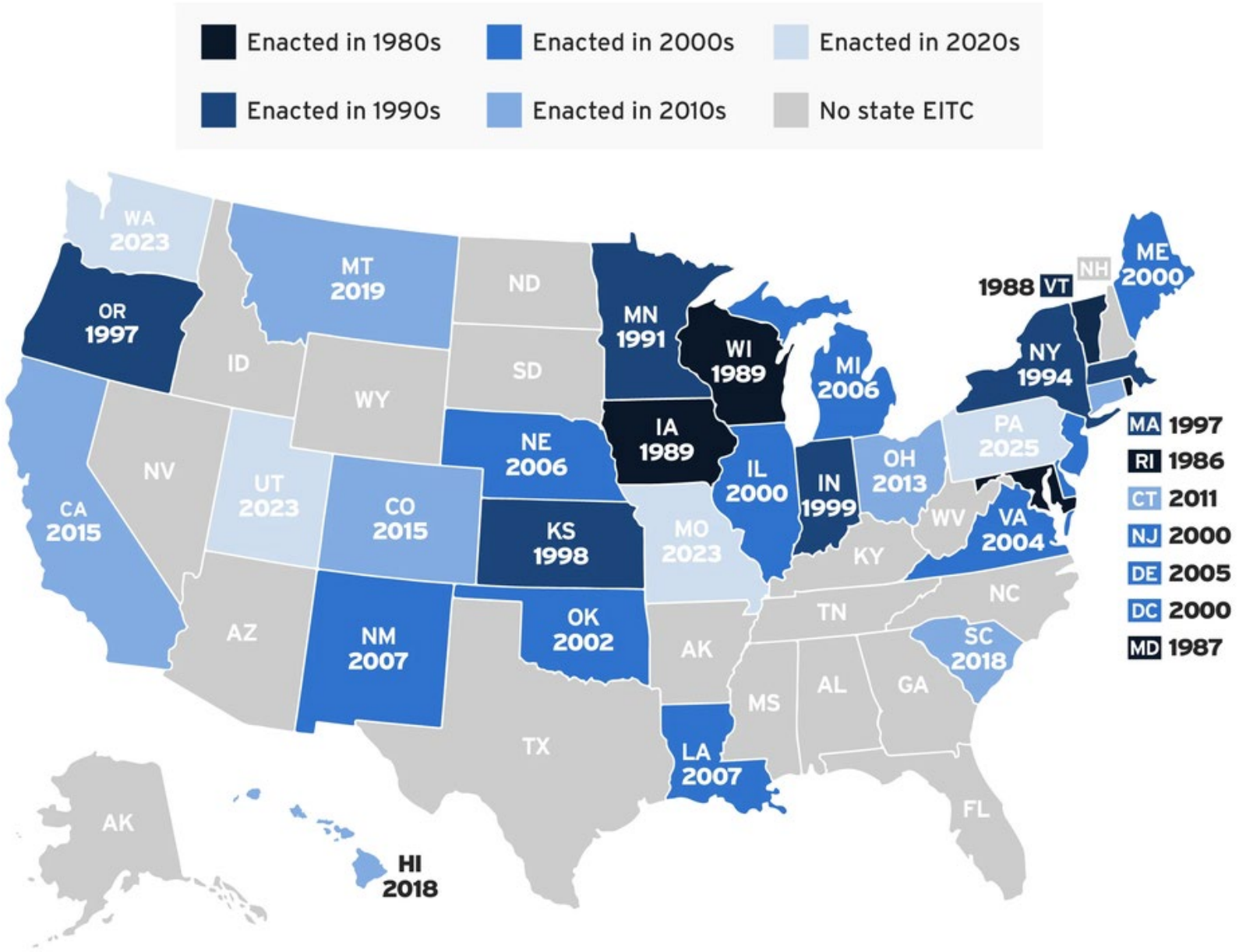


Source: Institute on Taxation and Economic Policy, January 2024.

New Mexico provides a significant baseline exemption from income tax

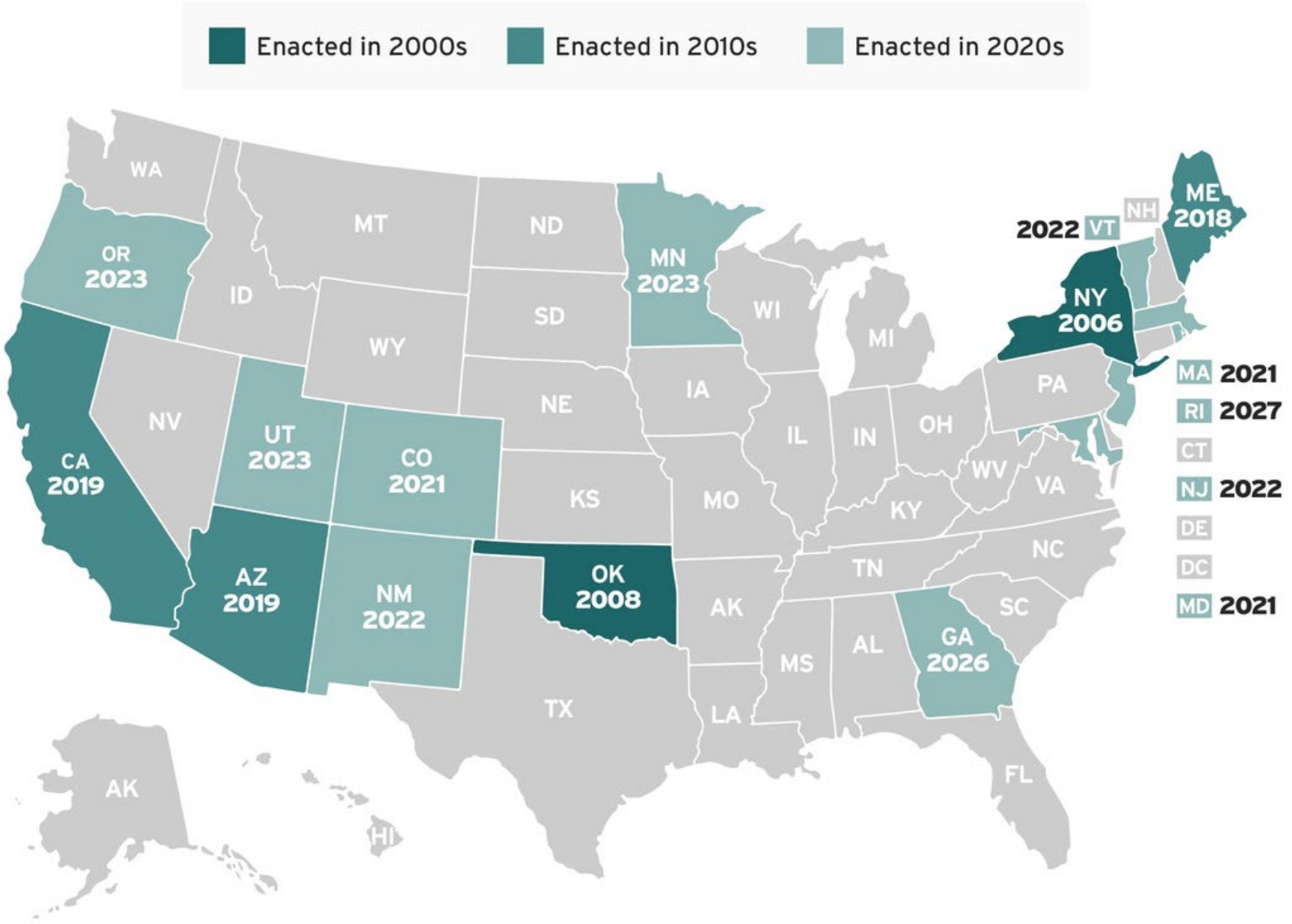


State Earned Income Tax Credits (EITC) are now the norm



Source: Institute on Taxation and Economic Policy

State Child Tax Credits are increasingly common



Source: Institute on Taxation and Economic Policy

The “No Tax on _____” Movement

Tips

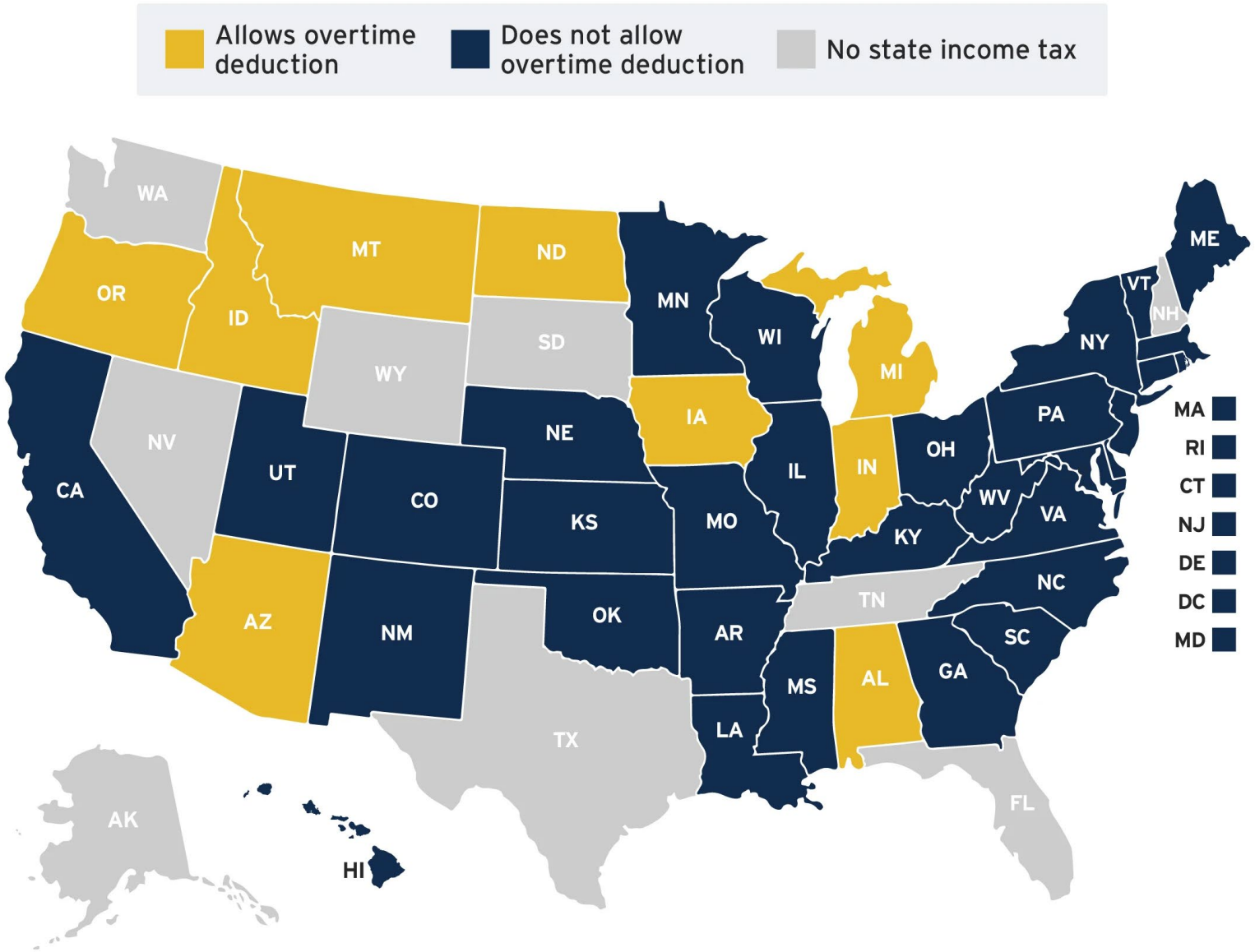
Overtime

Social Security

Retirement income

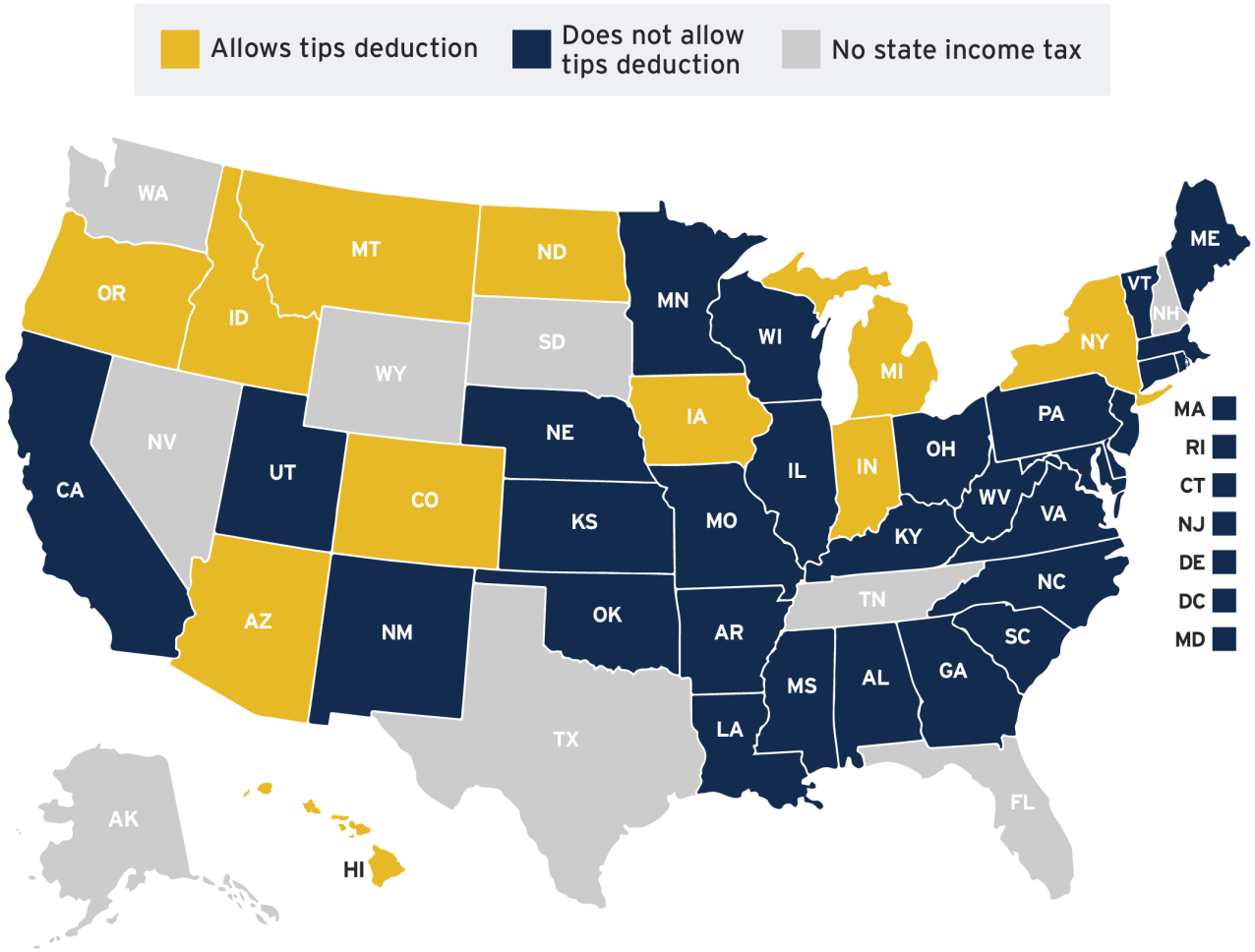
Etc.

State Overtime Pay Deductions



Source: Institute on Taxation and Economic Policy

Which States Allow Deductions for Tipped Income in 2026?



Examples of eligible jobs, per IRS:

- Wait staff and bartenders
- Taxi and rideshare drivers
- Barbers
- HVAC installers
- Social media influencers
- Clowns and magicians
- Santa Claus impersonators

And examples of ineligible ones:

- Cashiers and desk clerks
- Retail security guards
- Childcare workers
- Home health aides

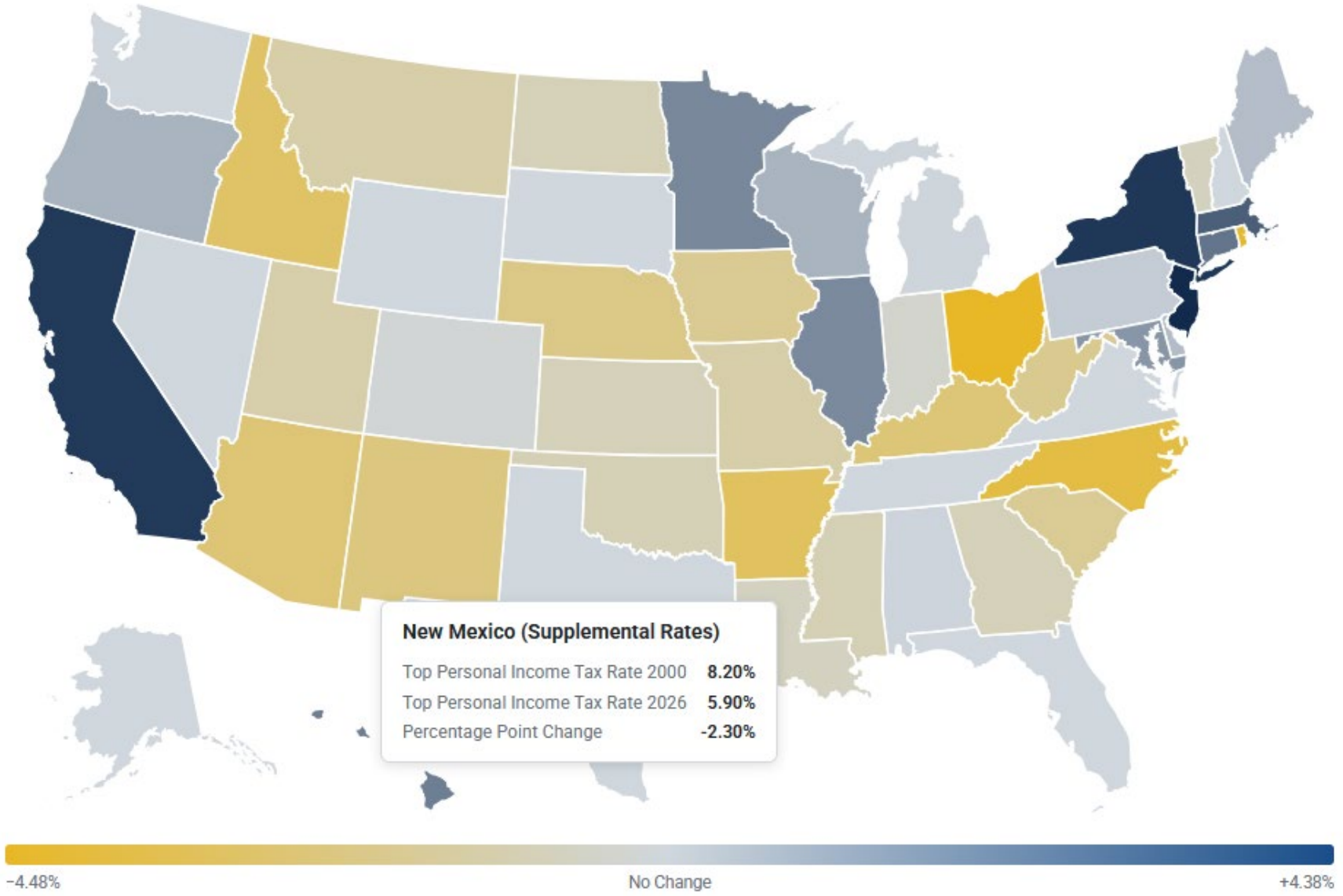
ITEP.org

Source: Institute on Taxation and Economic Policy

Questions?

Changes in Top State Personal Income Tax Rates this Century

(2000-2026)



Source: ITEP Historical Tax Rate Data

What Does the Best Available Evidence Tell Us About State Taxes and Growth?

- "The effects of taxes on state-level growth have been the subject of continuing controversy, with many conflicting and fragile results in the literature."
  - William G. Gale, Aaron Krupkin, and Kim Reuben, in National Tax Journal

- "…Some studies by reputable economists that find that above-average state and local taxes have a measurable and consistently adverse impact on state economic performance. However, many equally reputable studies reach the opposite conclusion, and the results of many more are mixed, ambivalent, or show that any adverse impacts are small. There is simply no consensus…"
  - Michael Mazerov, Center on Budget and Policy Priorities

State Actions to Tax the Rich in 2026

Tax rate increase, and taxable income levels, at which new/higher rates take effect

New millionaires' brackets:

1. Washington State (9.9%; $1M+)
2. Rhode Island (3%; $1M+)
3. Hawai‘i (2%; $1M+)
4. Maine (2%; $1M+)

Other new high-income taxes:

5. California (2%; $743,000+)
6. Colorado (4%; $500,000)

Recent State Actions to Tax the Wealthy with Tailored Income Tax Reforms

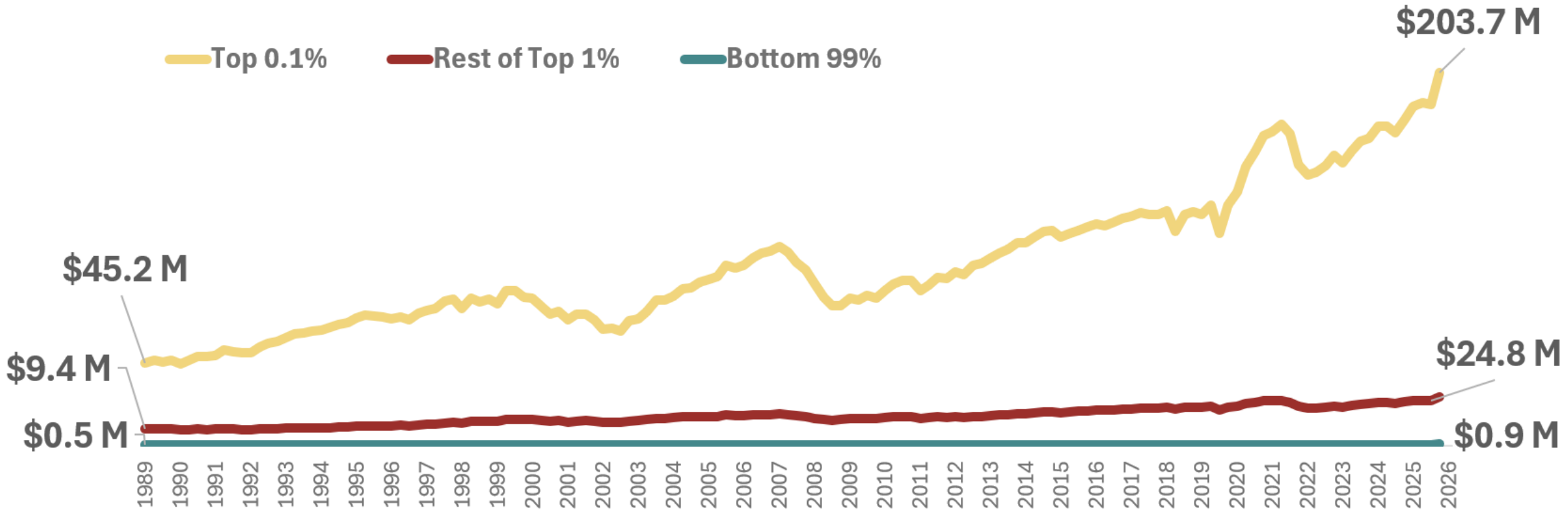
2021: Washington State's 7% capital gains tax on gains over $250,000

2023: Minnesota's 1% tax on investment returns over $1M

2025: Maryland's 2% tax on capital gains if income is over $350,000

Average Wealth, by Wealth Percentile

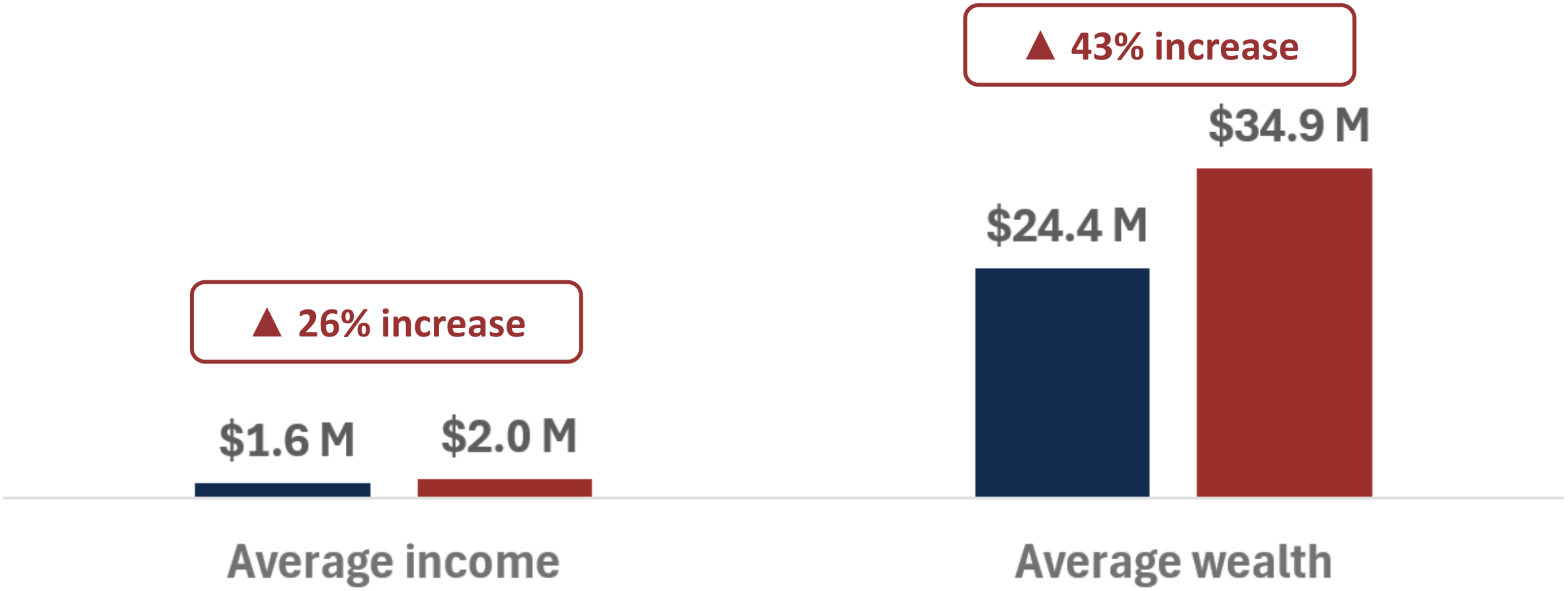
$millions, adjusted for inflation



Source: ITEP analysis of Federal Reserve data

Top 1% Average Income and Wealth, 2013-2023

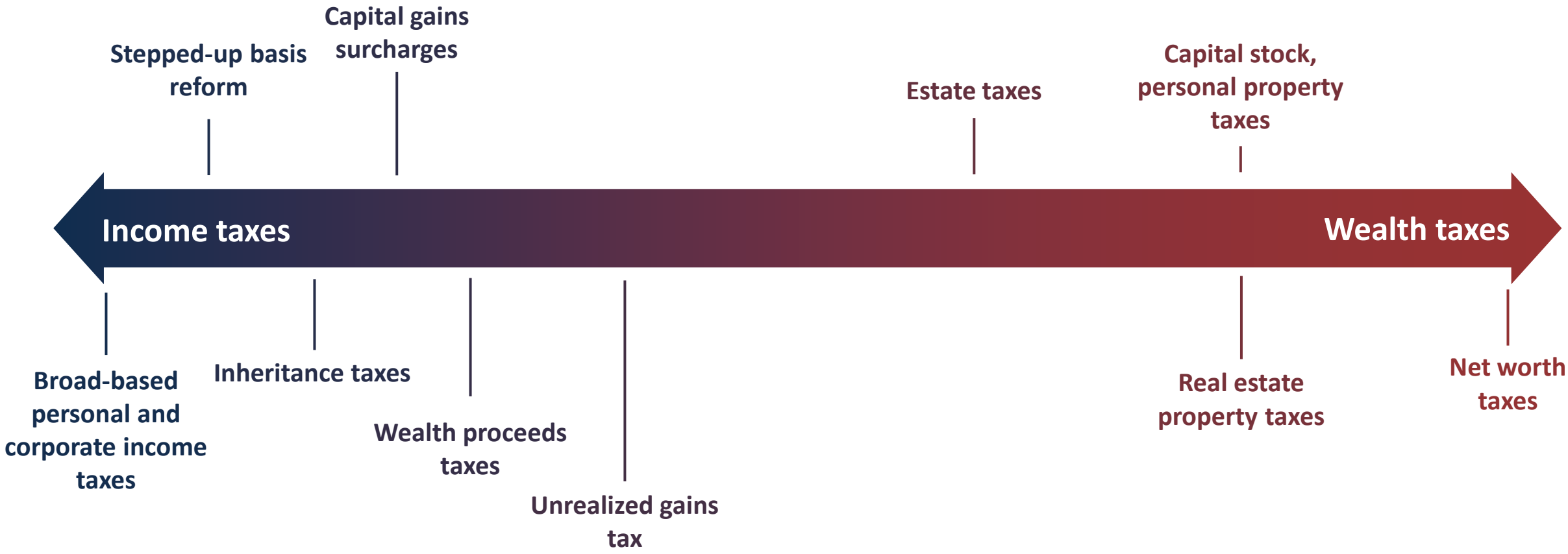
$millions, adjusted for inflation



Source: ITEP analysis of IRS and Federal Reserve data

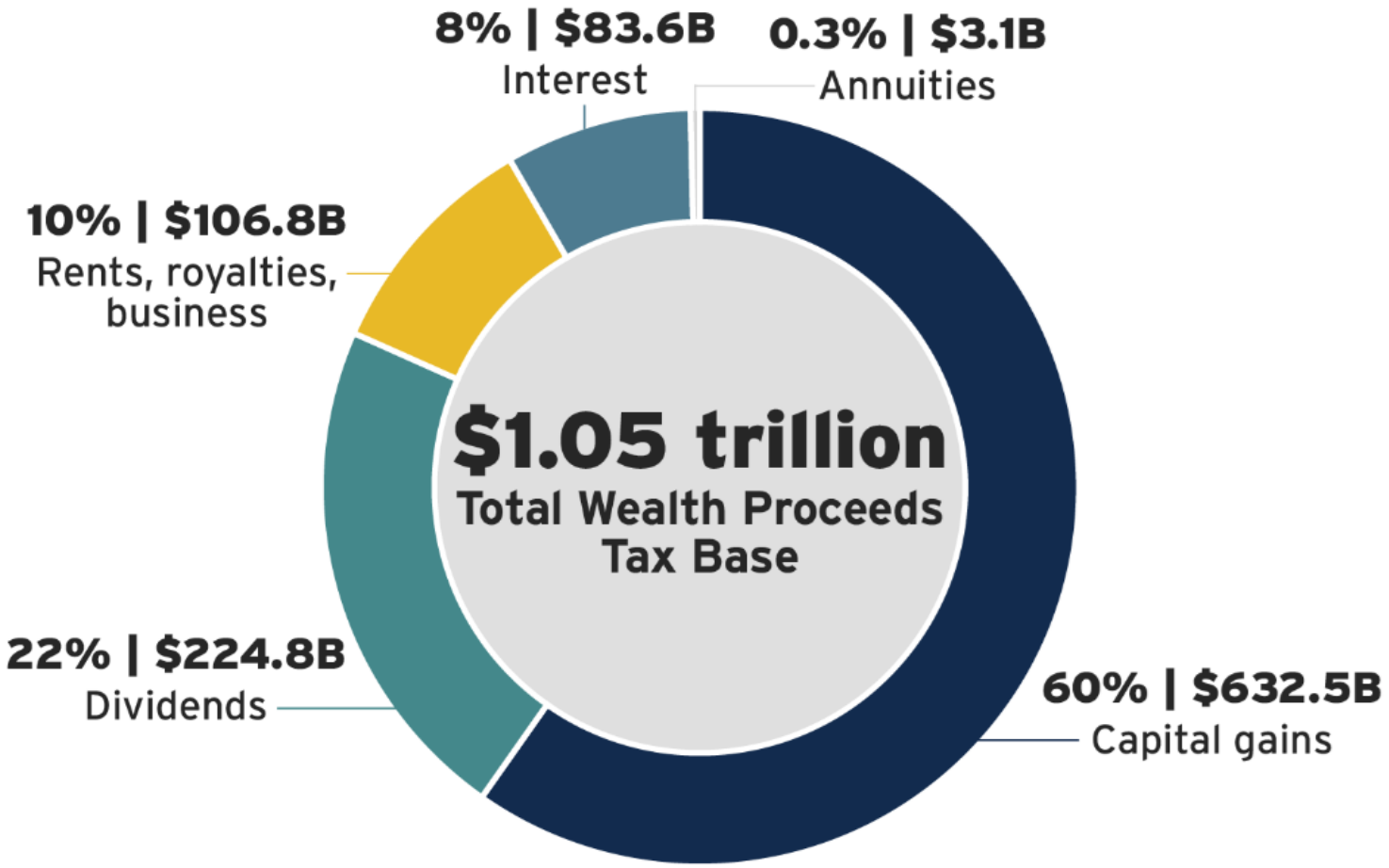
A Continuum of Policy Options: From Income to Wealth Taxation

(This is a thought experiment to spark discussion; sorting is not scientific and not legal advice)



Components of State Wealth Proceeds Tax Bases

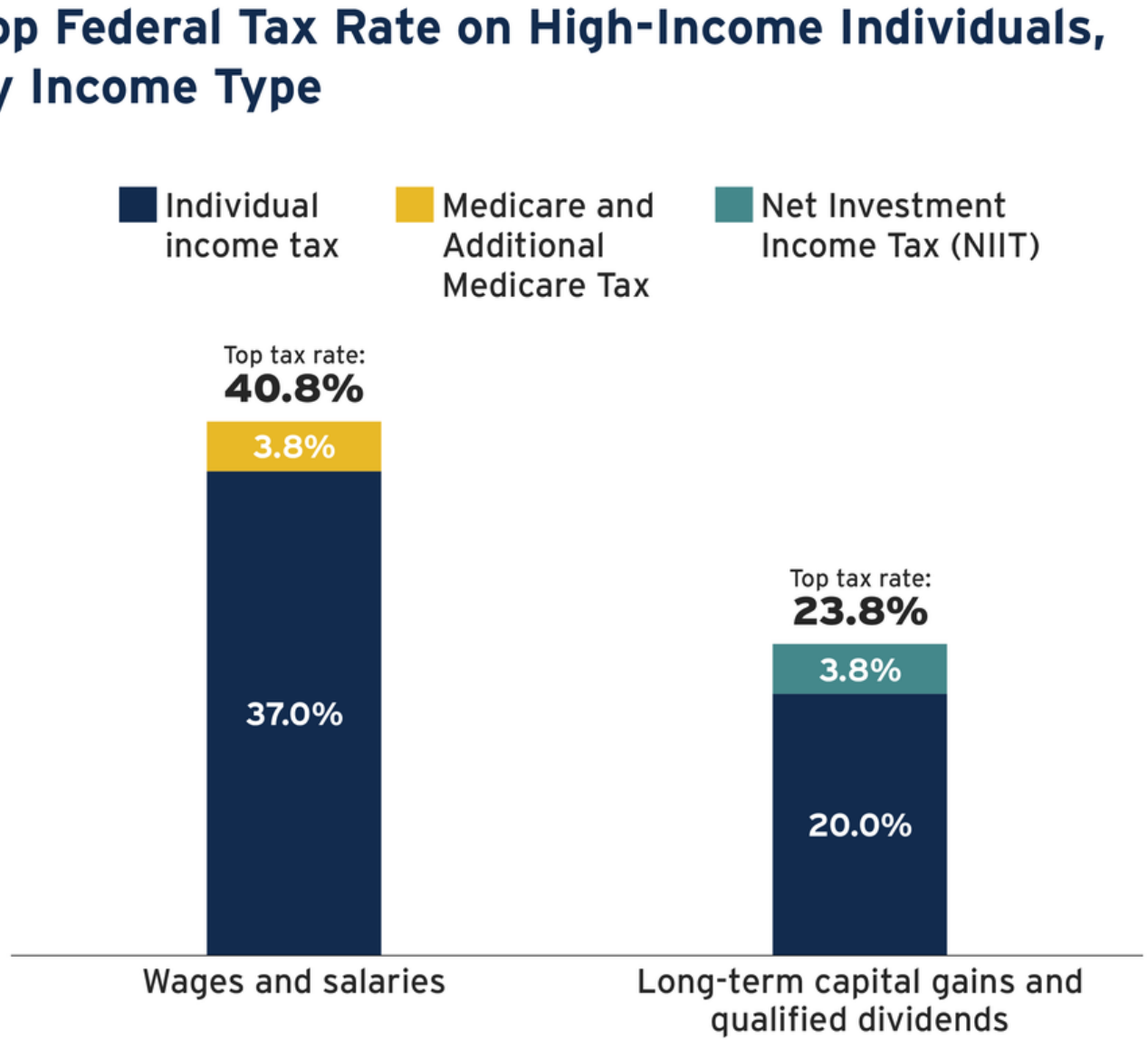
National figures



Source: Institute on Taxation and Economic Policy

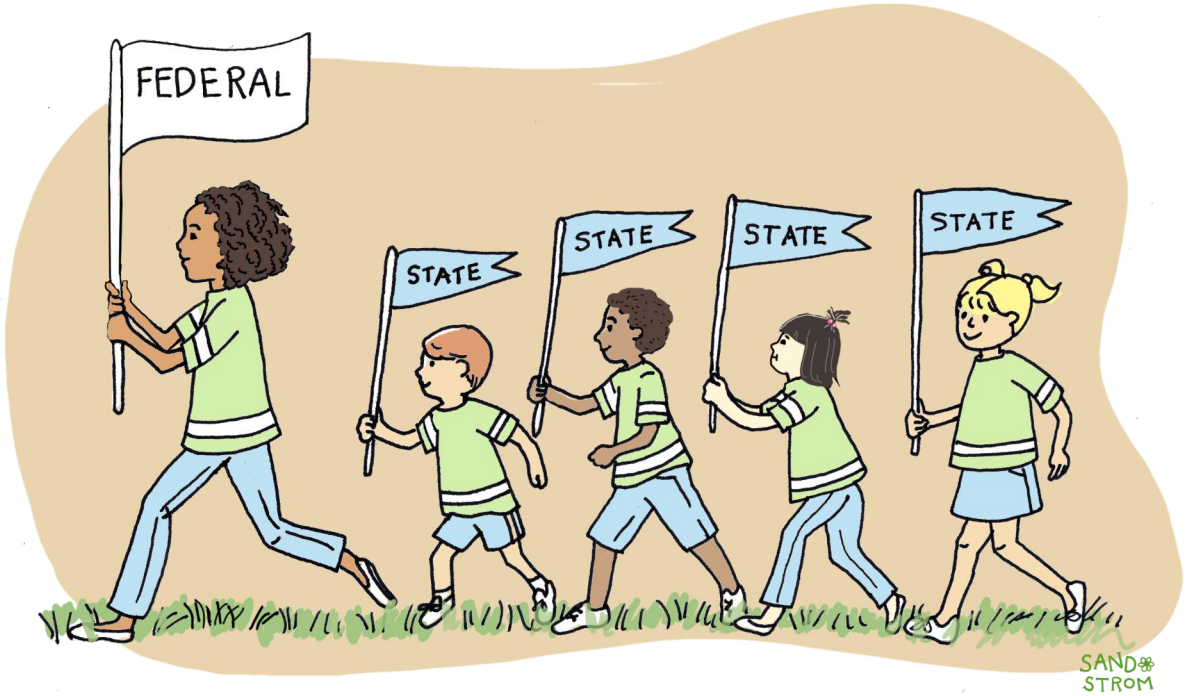
Some states are interested in this because they object to federal tax carveouts for investment income such as:

- Preferential tax rates
- Stepped-up basis
- Deferral of tax until realization
- QSBS and other exemptions



Source: Institute on Taxation and Economic Policy

Questions?



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The ITEP Guide to State & Local Taxes

How Does Federal-State Tax Conformity Work?

Most states use the federal tax code as a starting point for their calculations of state personal income taxes, corporate income taxes, and estate taxes.

Changes to the federal code and federal tax administration have the potential to affect state tax systems enormously, but to some extent states can pick and choose which of those federal changes to accept.

Personal income tax:

New Mexico ⟷ Federal connections



Adjusted Gross Income (AGI)	Standard / Itemized Deds.	Earned Income Tax Credit (EITC)

Personal income tax:

H.R. 1 items now in New Mexico tax law



Adjusted Gross Income (AGI)

- Expanded dep. care FSAs
- Trump accounts
- Opportunity Zones
- QSBS
- 529 accounts (priv. K-12)

Standard / Itemized Deds.

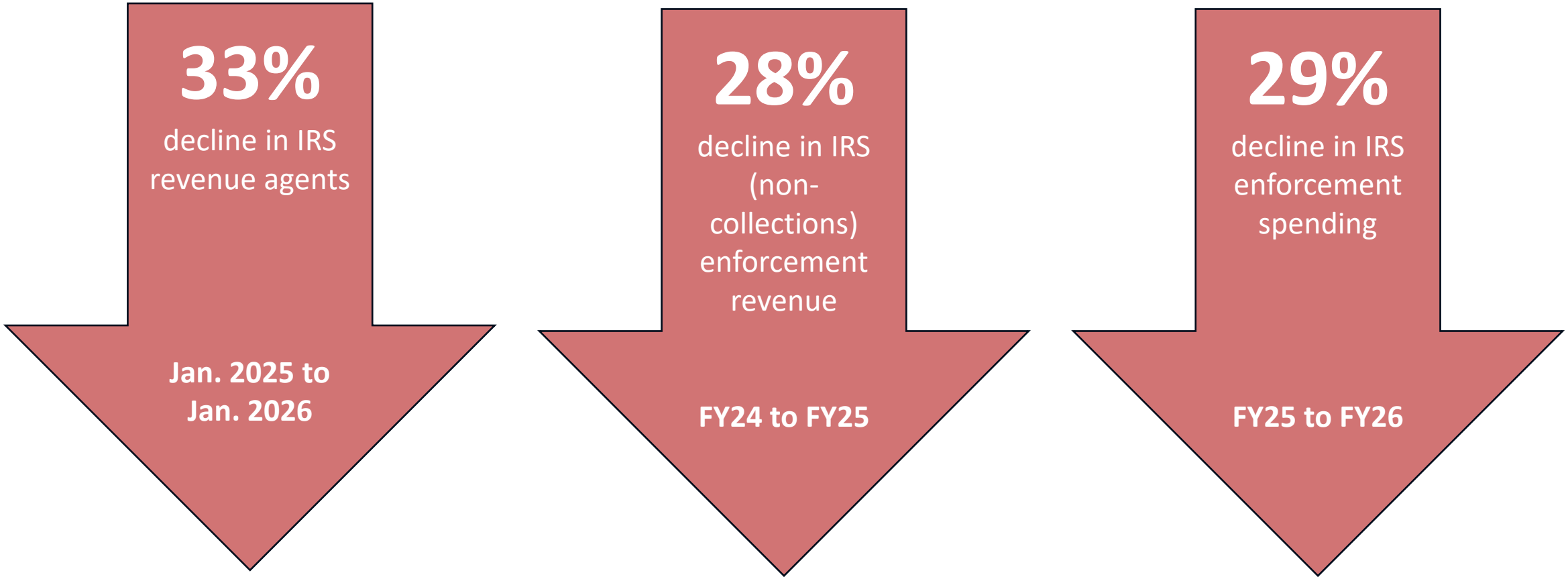
- ~5% boost to standard seduction
- SALT cap increase ($10,000 to $40,400)
- Floor on charitable deduction (0.5% of AGI)
- ~5% itemized ded. limit (2/37ths)

Earned Income Tax Credit (EITC)

- N/A

Questions?

Declines in Federal Tax Enforcement



Source: Treasury Inspector General for Tax Administration



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