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## FISCAL IMPACT REPORT



SPONSOR: Mohorovic DATE TYPED: 2/04/02 HB 284

SHORT TITLE: Reduce Personal Income Tax Rates SB \_\_\_\_\_

ANALYST: Smith

### REVENUE

Estimated Revenue		Subsequent Years Impact	Recurring or Non-Rec	Fund Affected
FY02	FY03			
	(\$31,980.0)		Recurring	General Fund

(Parenthesis ( ) Indicate Revenue Decreases)

Duplicates SB 209

### SOURCES OF INFORMATION

Taxation and Revenue Department (TRD)

### SUMMARY

#### Synopsis of Bill

This measure would reduce New Mexico personal income tax rates in a way that would provide tax decreases averaging 3 percent for New Mexico taxpayers. The current and proposed rate structures are shown below. Threshold amounts for tax rate brackets would not be modified.

### FISCAL IMPLICATIONS

The estimate shown overstates the decrease in General Fund revenue by approximately 5% due to the "state deduction recovery". Because state taxes are deductible from federal taxable income for taxpayers who itemize deductions, and state taxes "piggyback" on the federal income measure, state taxes are effectively deductible from their own tax base. In this case, when state tax liability is reduced, the amount deducted from taxable income is reduced, with the result that liabilities increase slightly, thus offsetting a portion of the initial reduction.

**OTHER SUBSTANTIVE ISSUES**

TRD makes the following observations:

As shown in the final column of the table below, the proposed measure would provide the largest absolute reduction in taxes to individuals with taxable incomes in excess of \$75,000 annually. However, the greatest percentage reduction in taxes would accrue to individuals with taxable incomes below \$15,000. The total reduction in taxes per return would be approximately \$54. The personal income tax currently generates approximately \$1 billion annually. Since the state's population is currently roughly 1.8 million, personal income tax obligations average roughly \$555 per person statewide. The proposed measure would reduce this figure by approximately \$16.70.

Estimated Full Year Effects of Proposed Tax Rate Reduction							
Taxable Income			Estimated Gross Liability Under Present Law (\$Millions)	Proposed Liability (\$Millions)	Decrease (\$Millions)	Percent of Current Liability	Decrease Per Return
\$0	to	\$15,000	40.5	39.3	1.2	2.9	\$5
\$15,000	to	\$25,000	77.3	75.1	2.2	2.8	\$23
\$25,000	to	\$40,000	154.0	149.4	4.5	2.9	\$48
\$40,000	to	\$75,000	300.8	292.2	8.7	2.9	\$94
\$75,000		and over	509.9	493.6	16.2	3.2	\$350
<b>Totals</b>			<b>1,082.4</b>	<b>1,049.6</b>	<b>32.8</b>	<b>3.0</b>	<b>\$56</b>

Because the state's tax brackets are not indexed for inflation, personal income tax collections typically increase as a percent of personal income over time. This effect is commonly called "bracket creep". Due to bracket creep, annual personal income tax revenues increased by over \$500 million during the last ten years -- an increase of over 100 percent. Total personal income received by New Mexico residents increased by about 63 percent during the same period. New Mexico personal income tax collections therefore increased from about 1.8 percent of personal income to 2.3 percent of personal income during the period. In the absence of bracket indexing, the only way to avoid increasing personal income taxes as a percent of personal income is to periodically reduce rates or shift brackets upward. The proposed bill employs the first approach.

SS/njw:ar