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

SPONSOR: Robinson DATE TYPED: 2/14/03 HB

SHORT TITLE: Net Capital Gain Deduction for Business Sale SB 442

ANALYST: Smith

REVENUE

Estimated Revenue		**Subsequent Years Impact**	**Recurring or Non-Rec**	**Fund Affected**
FY03	**FY04**			
	(1,140.0)	(2,330.0)	Recurring	General Fund

(Parenthesis ( ) Indicate Revenue Decreases)

SOURCES OF INFORMATION

Responses Received From

TRD

SUMMARY

Synopsis of Bill

Senate Bill 442 proposes to eliminate the state personal income tax on net capital gains income attributable to the sale of a closely-held business. Under present law taxpayers can deduct up to $1,000 per year in net capital gains income. The proposal would modify the present law language to allow a deduction for “the greater of” the current deduction or the taxpayer’s net capital gain from a closely-held business. To qualify for the deduction a taxpayer must sell (1) their entire interest in the business in a transaction in which substantially all of the equity interests are sold, or (2) the business must effectively sell all of its assets.

FISCAL IMPLICATIONS

TRD notes the estimate assumes New Mexico realized net capital gains will total $1 billion annually, and that of this amount, 3.4 percent or $34 million will result from the sale of closely held businesses. The 3.4% is drawn from I.R.S. data on the share that small business interests represent in the composition of assets in estate tax returns. Multiplying by an average tax rate of 7.0 percent results in the $2.38 million amount when fully phased in. The fiscal impact was reduced to reflect the deductibility of $50 thousand per year by the affected taxpayers under present law. Annual gains from the value of businesses tend to vary widely from year to year.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

This bill would conflict with both HB167 and SB167.

OTHER SUBSTANTIVE ISSUES

TRD notes that SB 442 discriminates against interstate commerce because it applies only to capital gains that would be allocated or apportioned to New Mexico. The remedy to this problem would be to make the deductions available to all taxpayers with gains from a closely-held business.

Under federal income tax statutes, state income tax payments are deductible for purposes of calculating federal income tax. Thus, because this proposal would reduce state income tax liabilities, it would also reduce these deductions, thereby increasing the taxpayer’s federal income tax liability. This reduces the net benefits of the tax reduction for the taxpayer. For example, if a taxpayer is in the 30% tax bracket, the net benefit to the taxpayer of the state tax reduction would be reduced by 30%.

SS/njw