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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: 2/05/04 HB

SHORT TITLE: Income Tax Deduction for Business Sale SB 411

ANALYST: Taylor

REVENUE

Estimated Revenue		Subsequent Years Impact	Recurring or Non-Rec	Fund Affected
FY04	**FY05**			
	(2,900.0)	(2,400.0)	Recurring	General Fund

(Parenthesis ( ) Indicate Revenue Decreases)

SOURCES OF INFORMATION

LFC Files

Responses Received From
Taxation and Revenue Department

SUMMARY

Senate Bill 411 proposes an income tax deduction for net capital gain income from the sale of a closely held trade or business. The size of the deduction is equal to the taxpayer's net capital gain from the sale of a closely held trade or business in the taxable year for which the deduction is being claimed, provided that the gain is included in the taxpayer's base income.

A closely held trade or business is defined to mean a trade or business operated as a sole proprietorship or a corporation, partnership, limited partnership, limited liability company or other legal entity, whose equity is controlled by 75 or few qualifying owners.

FISCAL IMPLICATIONS

TRD estimates that this bill will reduce general fund revenues by $2.9 million in FY05. The estimate assumes net capital gains in New Mexico will total approximately $1.5 billion annually, and further estimated that of 3.4 percent of this was this, or $50 million was from the sale of closely held businesses. They report that 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. They also note that 10 percent of capital gains will be deductible in 2004. This leaves a base of $45 million, and a revenue loss of $2.9 million in FY05 (implying an average of rate of 6.4 percent). The revenue loss decreases over time, reflecting the phased-in income tax rate reductions.

ADMINISTRATIVE ISSUES

TRD reports modest administrative impacts that can be absorbed with existing resources.

TECHNICAL ISSUES

TRD provided the following technical issues:

1. The proposal should have an applicability date explaining to which tax years the proposed policy applies.
2. As currently written, SB 411 would appear to violate the Commerce Clause since it discriminates against interstate commerce by applying 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.

BT/lg