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FISCAL IMPACT REPORT

ORIGINAL DATE 2/28/07

SPONSOR Jennings LAST UPDATED _____ HB _____

SHORT TITLE Income Tax Reductions and Rebates SB 1185

ANALYST Francis

APPROPRIATION (dollars in thousands)

Appropriation		Recurring or Non-Rec	Fund Affected
FY07	FY08		
299,690.0		Nonrecurring	General Fund

(Parenthesis () Indicate Expenditure Decreases)

REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Non-Rec	Fund Affected
FY07	FY08	FY09		
(209,200.0)	(109,300.0)		Nonrecurring	General Fund
	(27,900.0)	(29,100.0)	Recurring	General Fund

(Parenthesis () Indicate Revenue Decreases)

SOURCES OF INFORMATION

LFC Files

Responses Received From

Taxation and Revenue Department (for similar bills)

SUMMARY

Synopsis of Bill

Senate Bill 1185 combines several revenue related changes with capital outlay appropriations.

SUMMARY:

- Decreases personal income tax rate for top income bracket to 4.9 percent.
- Enacts a Working Families Tax Credit (WFTC) that is 10 percent of the Federal Earned Income Credit (EIC).
 - Redefines modified gross income to exclude credits
 - Disallows low-income comprehensive tax credit (LICTR) if WFTC claimed
- Provides a tax rebate of \$138 per exemption claimed to all NM resident taxpayers

- Exempts the rebate from state tax
- Inmates and non residents excluded
- Appropriates \$300 million for capital outlay projects

Personal Income Tax Rate Reduction. This section accelerates the current phase-in of the personal income tax rate reductions. Under current law, the top personal income tax rate will be 5.3 percent in tax year 2007 and 4.9 percent in 2008. This bill would accelerate the schedule so the rate would be 4.9 percent in 2007 forward, a reduction of 0.4 percent in the top personal income tax rate in 2007. This is effective January 1, 2007.

Table 1: Tax Rate Cut

Tax Year	Current Law	SB265
2006	5.3%	5.3%
2007	5.3%	4.9%
2008	4.9%	4.9%

Working Families Tax Credit. This section creates a new personal income tax credit called the “Working Families Tax Credit” (WFTC) that is calculated as 10 percent of the federal Earned Income Credit (EIC). The credit is refundable, meaning if the credit exceeds the taxpayer’s liability, the excess is refunded to the taxpayer. SB 1185 also amends the low-income comprehensive tax rebate (LICTR) to make a taxpayer ineligible for LICTR if the taxpayer receives the WFTC. SB 1185 also explicitly excludes credits provided in the Income Tax Act from the calculation of modified gross income. The effective date is January 1, 2007.

Personal Income Tax Rebate. Senate Bill 1185 creates a personal income tax rebate for all NM residents who filed a tax return in 2006 who are not dependents of another taxpayer and who are residents on the last day of 2006 or for NM residents who file a tax return in 2007 provided they are a resident on the last day of 2007. The rebate amount is \$138 per exemption declared for federal income tax purposes. For those taxpayers who filed a return in 2006, the rebate is an advanced rebate that will be issued no later than June 30, 2007. For those taxpayers who did file a return in 2007 and did not receive an advance payment, the rebate can be claimed on the 2007 tax return. Either way, the rebate is exempt from NM personal income taxes.

FISCAL IMPLICATIONS

SUMMARY OF FISCAL IMPACTS (ALL GENERAL FUND)

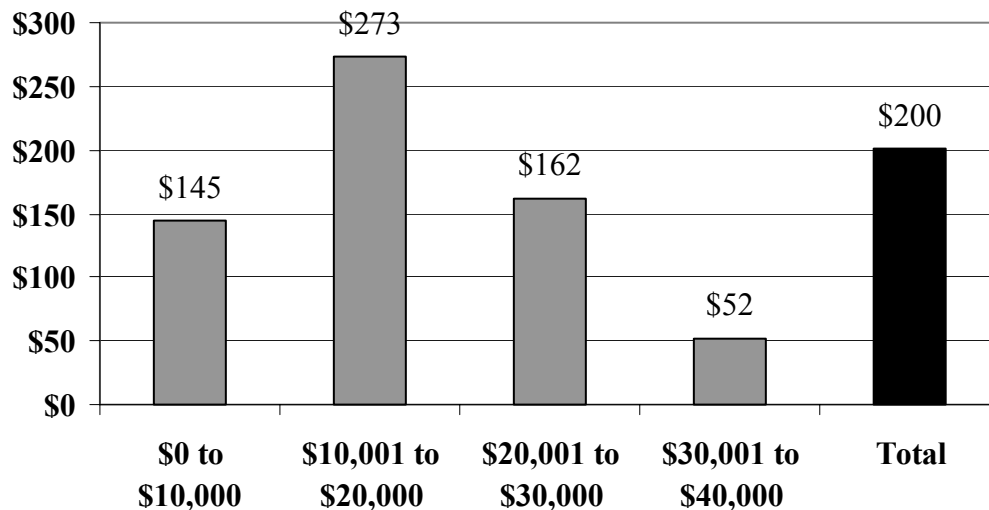
(\$M)	FY07	FY08	FY09
Accelerate PIT	(19.8)	(46.2)	
Working Families Tax Credit		(27.9)	(29.1)
Tax Rebate	(189.4)	(63.1)	
Recurring Revenue Changes	-	(27.9)	(29.1)
Nonrecurring Revenue Changes	(209.2)	(109.3)	-
Capital Outlay	300.0		

Personal Income Tax Rate Reduction. Using a model provided by the Taxation and Revenue Department (TRD), the full year impact would be a \$66 million reduction in personal income tax collections. Thirty percent of the impact, or \$19.8 million, occurs in FY07 because the first quarter of 2007 personal income tax collections will have been at the current rates. In FY08, the impact is \$46.2 million or 70 percent of the tax year impact. While this would reduce current estimates of recurring general fund revenues, the reduction is only for these two fiscal years and does not recur in the future.

Working Families Tax Credit. Enacting this credit would reduce general fund personal income tax revenue by \$30 million per tax year. Even though the credit is for tax year 2007, it is assumed that it will be claimed in the filing season in 2008 and so all of the impact is in FY08. The credit is expected to grow to \$30.2 million in FY09.

In 2004, 199,552 New Mexican taxpayers received the federal EIC and 90 percent of the credits were in excess of liability. A total of \$364 million in EIC were claimed. Using this number as the base, the cost to the state of the WFTC would be \$36.4 million. Some of those taxpayers would find it more beneficial to file for the LICTR and that would reduce the impact on the general fund to \$27.9 million. Figure one shows the total net benefit—the additional benefit of WFTC above LICTR—by income cohort. The average benefit for all taxpayers is \$200. Table two shows that 64 percent of the benefit goes to heads of household or single parents and most of them are in the \$10,001 to \$20,000 income range.

Figure One: Average Benefit by Income Cohort



Personal Income Tax Rate Reduction. In 2003, legislation was enacted lowering the top rate and collapsing the number of income brackets. In 2002, the top rate on taxable income over \$100,000 for married filers and \$65,000 for single filers was 8.2 percent. As a result of the 2003 legislation, by tax year 2007, the top rate would decrease to 4.9 percent and the top income bracket would begin at \$24,000 in taxable income for married filers and \$16,000 for single filers. In the 2005 session, the phase-in schedule for the top rate decrease was delayed until 2008 and the head-of-household filing status was merged with the married filing jointly status. The schedule was modified again in the 2005 special session as revenues came in stronger than expected. This bill restores the final phase-in year to 2007 rather than 2008. See table one for details about the changes to the personal income tax law over the last four years.

Table 1: Proposed Rate Schedule
Taxable Income

Married Filing Jointly, Surviving Spouses, Head of Household	Married Filing Separate	Single	2005	2006	2007	2008
<8000	<4000	<5500	1.7%	1.7%	1.7%	1.7%
8000-16000	4000-8000	5500-11000	3.2%	3.2%	3.2%	3.2%
16000-24000	8000-12000	11000-16000	4.7%	4.7%	4.7%	4.7%
24000+	12000+	16000+	5.7%	5.3%	4.9%	4.9%

Based on 2005 tax return data, a married filing jointly taxpayer reporting \$24 thousand in taxable income has total adjusted gross income (AGI) of about \$40 thousand. For singles reporting taxable income of \$16 thousand, their AGI starts at \$25 thousand. 311,000 taxpayers will receive the benefit of the lower rate, all of them above these AGI levels.

Working Families Tax Credit. Twenty states, including the District of Columbia, currently offer a state level EIC (Colorado’s EIC is tied to their TABOR rules and so some years they do not allow the credit). The credit has proven to be a simple and efficient credit. It is also popular since it only goes to individuals and families with earned income. One of the key elements is the refundability of the credit: the taxpayer receives the full amount of the credit regardless of the tax liability. Twelve of the seventeen state EICs are refundable, according to research at the Institute on Taxation and Economic Policy. New York and Vermont have the most generous EICs allowing over 30 percent of the federal credit and making it refundable. Rhode Island has a 25 percent credit but it is not refundable which restricts its effectiveness.

TABLE 1: STATE EARNED INCOME TAX CREDITS BASED ON THE FEDERAL EITC			
State	Percentage of Federal Credit (Tax Year 2006 Except as Noted)	Refundable	Workers Without Qualifying Children Eligible?
Delaware	20%	No	Yes
District of Columbia	35%	Yes	Yes
Indiana ^a	6%	Yes	Yes
Illinois	5%	Yes	Yes
Iowa	6.5%	No	Yes
Kansas	15%	Yes	Yes
Maine	5%	No	Yes
Maryland ^b	20%	Yes	No
Massachusetts	15%	Yes	Yes
Michigan	10% (effective in 2008; to 20% in 2009)	Yes	Yes
Minnesota ^c	Average 33%	Yes	Yes
Nebraska	8%	Yes	Yes
New Jersey ^d	20%	Yes	No

TABLE 1: STATE EARNED INCOME TAX CREDITS BASED ON THE FEDERAL EITC			
State	Percentage of Federal Credit (Tax Year 2006 Except as Noted)	Refundable	Workers Without Qualifying Children Eligible?
New York ^{e, f}	30%	Yes	Yes
Oklahoma	5%	Yes	Yes
Oregon	5% (to 6% in 2008)	Yes	Yes
Rhode Island	25%	Partially ^g	Yes
Vermont	32%	Yes	Yes
Virginia	20%	No	Yes
Wisconsin	4% - one child 14% - two children 43% - three children	4% - one child 14% - two children 43% - three children	No

Notes: From 1999 to 2001, Colorado offered a 10% refundable EITC financed from required rebates under the state's "TABOR" amendment. Those rebates, and hence the EITC, were suspended beginning in 2002 due to lack of funds and again in 2005 as a result of a voter-approved five-year suspension of TABOR. Under current law, the EITC is projected to resume in 2010.

a Presently scheduled to expire in TY 2011.

b Maryland also offers a non-refundable EITC set at 50 percent of the federal credit. Taxpayers in effect may claim either the refundable credit or the non-refundable credit, but not both.

c Minnesota's credit for families with children, unlike the other credits shown in this table, is not expressly structured as a percentage of the federal credit. Depending on income level, the credit for families with children may range from 25 percent to 45 percent of the federal credit; taxpayers without children may receive a 25 percent credit.

d The New Jersey credit is available only to families with incomes below \$20,000.

e The New York credit would be reduced automatically to the 1999 level of 20 percent should the federal government reduce New York's share of the TANF block grant.

f Beginning in 2006, New York also allows certain non-custodial parents who are making child support payments to claim an EITC that is the greater of 20 percent of the federal EITC that they would be eligible for with one qualifying child as a custodial parent or 250 percent of the federal EITC for taxpayers without qualifying children.

g Rhode Island made a very small portion of its EITC refundable effective in TY 2003. In 2006, the refundable portion was increased from 10 percent to 15 percent of the nonrefundable credit (i.e. 3.75 percent of the federal EITC).

Source: Economic Policy Institute (www.epi.org)

For a single or married taxpayer with no children, the cut-off for benefits is very low but for taxpayers with children, the benefit goes to many more. The federal EIC can only be claimed if someone is below the income cut-offs and

- has a valid social security number
- is not filing separately
- is a US citizen or resident alien
- does not have foreign income
- does not have more than \$2,800 in investment income
- has some earned income.

Table one shows the cut-off and peak amounts and the maximum credit for each class of filer. For example, a married filer with one child and adjusted gross income of between \$8,000 and \$16,500 would receive the maximum federal credit of \$2,747 (state credit = \$275). The same filer with income over \$34,001 in adjusted gross income would receive no federal credit and, thus, no state credit.

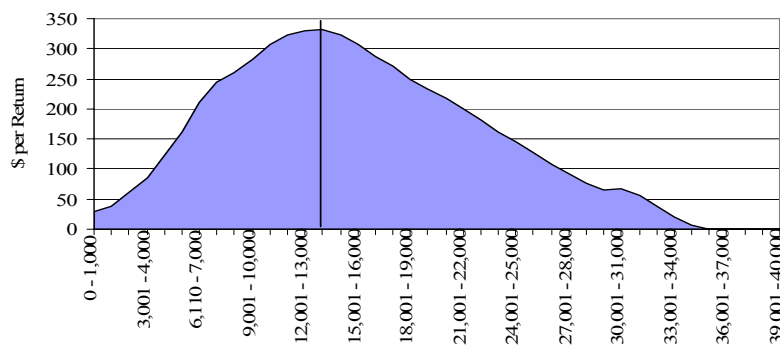
Table 1: Federal Income Cut-offs for Earned Income Credit

	Cut-off	Adjusted Gross Income Peak		Maximum Credit
		Start	Finish	
		Single		
No children	12,120	5,500	6,500	412
One child	32,001	8,500	14,500	2747
More than one child	36,348	11,500	14,500	4536
Married				
No children	14,120	5,500	8,500	412
One child	34,001	8,000	16,500	2747
More than one child	38,348	11,500	16,500	4536

Source: IRS 2006 Tax Year

For filers without children, they must be age 25 to 65, not a qualifying child or dependent of another person and must have lived in the United States for more than six months. For filers with children, the children must be younger than 19, younger than 25 if a full time student, or permanently disabled. The children also have to have lived with the filer for more than six months and cannot be claimed as a qualifying child or dependent of another person.

Figure Two: Working Families Tax Credit Phase-out



Source: TRD

One of the features of the EIC is that it phases-out at higher incomes. Figure two, which is based on 2005 data, shows the maximum average credit of about \$325, which would be \$3,250 for the federal EIC, is reached at an income level of \$13,000. This is an average of all tax filers, whether single or not or childless or not.

Table 2: Average Benefit by Filing Status and Income

	Total Benefits	Number of Returns	Average Benefits per Return	Share of Total Benefits
Single				
\$0 to \$10,000	\$594,047	6,984	\$85	5%
\$10,001 to \$20,000	\$872,052	3,861	\$226	3%
\$20,001 to \$30,000	\$141,349	1,036	\$136	1%
\$30,001 to \$40,000	\$1,813	35	\$52	0%
Total	\$1,609,261	11,916	\$135	9%
Married Joint				
\$0 to \$10,000	\$881,612	5,632	\$157	4%
\$10,001 to \$20,000	\$4,348,460	14,831	\$293	11%
\$20,001 to \$30,000	\$2,998,852	16,593	\$181	12%
\$30,001 to \$40,000	\$265,967	4,901	\$54	4%
Total	\$8,494,891	41,957	\$202	30%
Head of Household				
\$0 to \$10,000	\$2,917,551	17,693	\$165	13%
\$10,001 to \$20,000	\$11,034,522	40,760	\$271	29%
\$20,001 to \$30,000	\$3,754,323	24,982	\$150	18%
\$30,001 to \$40,000	\$97,982	2,046	\$48	1%
Total	\$17,804,378	85,481	\$208	61%
All returns				
\$0 to \$10,000	\$4,393,210	30,309	\$145	22%
\$10,001 to \$20,000	\$16,255,034	59,452	\$273	43%
\$20,001 to \$30,000	\$6,894,524	42,611	\$162	31%
\$30,001 to \$40,000	\$365,762	6,982	\$52	5%
Total	\$27,908,530	139,354	\$200	100%

Source: TRD

Personal Income Tax Rebate. SB1185 sets up a rebate similar to the one issued in 2005 by legislation enacted following the 2005 special session. Whereas that rebate had varying amounts depending on income and number of exemptions, this rebate is \$138 per exemption regardless of income. The rebate will reduce personal income tax revenues which flow to the general fund by \$243 million.

Assuming that 25 percent growth in tax returns based on the growth from 2004 to 2005, it is estimated that \$243 million will be included in the advanced payments and \$40 million will be claimed on the 2007 tax return in FY08. Over sixty percent of the rebates would go to those with less than \$35,000 in adjusted gross income. The average rebate per taxpayer is \$284.

Table 1: Average Rebate by Income

	Share	Average Rebate	Average Exemptions
0 to 10,000	17%	\$ 192.9	1.40
10,001 - 20,000	22%	282.8	2.05
20,001 - 35,000	22%	304.3	2.20
35,001 - 50,000	11%	319.6	2.32
50,001 - 100,000	22%	358.5	2.60
100,001 +	6%	379.4	2.75
All Taxpayers		284.1	2.06

LFC has calculated the impact at \$243 million using the number of exemptions from the 2005 tax return data and adjusting it for dependents. TRD has estimated the impact \$43 million lower at \$207 million using information from the 2005 rebate.

Capital Outlay:

AGENCY	REASON	AMOUNT
Administrative Office of the Courts	Court of Appeals Building in Bernalillo	8.000
	Equipment for courtrooms, including security and interpreting equipment	4.000
Aging and Long Term Services	Equipment, vehicles and renovation to senior citizen centers statewide	8.200
Border Authority	Streets and drainage in Columbus port of entry	0.600
	Drainage study at Columbus port of entry	0.100
Commission for the Blind	Roof replacement/fire protection sprinklers	0.935
Corrections Department	Kitchen at Camino Nuevo facility	1.000
Cultural Affairs Department	Renovations/repairs to museums and monuments	5.000
	Construction completion of Hispanic Cultural Center	1.300
	Phase I construction of archaeology center in Santa Fe	1.800
	Upgrades/expansions to museum of space history in Alamogordo	1.200
	Complete phase I and II of the main gallery for farm and ranch heritage museum in Las Cruces	4.000
	Renovate Girard wing of International Folk Art Museum in Santa Fe	0.900
Cumbres & Toltec	Art collection/museum resources equipment including van of enchantment	0.750
	Locomotive/track improvements	2.000
Economic Development Department	Redevelopment of central business districts	2.000
	Utilities at Wood Cluster park in Las Vegas	0.500

AGENCY	REASON	AMOUNT
Public Education Department	Pre-K classrooms	3.000
	Laptop computers for 7th graders	1.500
	Library Books	2.000
	IT infrastructure	10.000
Office of State Engineer	Surface water measurement - Rio Gallinas/Rio Chama	3.000
Energy Minerals and Natural Resources Department	Fire trucks and carriers	0.500
	Park improvements	2.500
Department of Finance and Administration	Affordable housing	8.000
	Tribal water/wastewater and other infrastructure/economic development	7.000
	Home weatherization	2.000
Game/Fish	Lake Roberts and Burns Canyon dam repairs	3.300
Local Government Division	Public health facility renovation in Socorro	0.500
	Public health facility renovation in Gallup	0.500
	Public health facility renovation in Espanola	2.500
State Armory	Maintenance and renovations including Rio Rancho training center	3.000
Property Control Division	State laboratory	21.000
Department of Public Safety	Vehicle maintenance and replacement	1.500
Public School Capital Outlay	Local share for charter schools	10.000
	New/expanded facilities in high growth areas	40.000
	Supplemental funding to address adequacy	10.000
Public Regulation Commission	Firefighters training academy	0.535
State Fair	Various projects	10.000
Supreme Court Building Commission	Fire suppression and ADA compliance	1.000
Tourism	Gallup and Glen Rio visitor centers	0.750
Wastewater Facility Construction Loan Fund Capital Program Fund	Various projects	1.500
	Border authority office	0.300
	Renovations to youth diagnostic development center	4.000

AGENCY	REASON	AMOUNT
	Gym, weight room and vocational classrooms at juvenile facility in Dona Ana	5.000
	Upgrades to Eagle Nest reintegration center	0.500
	Upgrades to Camp Sierra Blanca	0.500
	Security upgrades at state-owned correctional facilities	6.000
	Repairs/maintenance of state-owned correctional facilities	5.000
	Renovations at Fort Stanton	0.500
	Purchase/installation of printing equipment for state printing office	0.500
	Purchase of Coughlin Building in Santa Fe	1.500
	Emergency repairs to state buildings	2.000
	HVAC upgrades to state buildings including Simms Building	6.000
	Structural/programmatic analysis of Department of Health facilities	0.500
	Medical and dental unit at Sequoyah facility	0.900
	Analytical equipment for scientific laboratory	1.300
	Alzheimer's unit at NM Veterans' home in T or C	1.800
	Improvements to state health facilities	6.000
	Epi Duran building in Las Vegas renovations	0.300
	Repairs/maintenance of offices in Alamogordo, TIWA building in Albuquerque and Las Cruces facility	1.500
	State police district office in Las Cruces	5.000
	State police district office in Las Vegas	5.000
	Port of entry in Lordsburg	12.000
	IT mitigation and facility renovations	1.000
	State crime laboratory	1.700
	Remittance transport replacement and security upgrades at Lujan building	0.600
NM School for the Blind	Early childhood center	6.000
NM School for the Deaf	Renovate Connor Hall and dining hall	6.700
UNM	Patient care equipment for UNMH and cancer treatment center	5.000
	Breast cancer research	3.215

AGENCY	REASON	AMOUNT
	Center for isotopes in medicine	3.500
SUB TOTAL		281.685
Contingent Appropriations		
Indian Water Rights Settlement Fund	Aamodt settlement	12.000
Pecos River Compact	Purchase land/water rights and development of augmentation well fields	3.000
	Purchase land/water rights and development of augmentation well fields	3.000
SUB TOTAL		18.000
GRAND TOTAL		299.69

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

SB 265 is a similar bill that cuts the personal income tax rate to 4.9 percent.

SB 317 as amended is a similar bill that enacts a WFTC but allows LICTR recipients to claim the WFTC and the percentage of the EIC is 7.5 percent.

SB812 is a similar bill that provides a tax rebate.

Capital outlay included in this bill will likely be similar to other legislation and the executive recommendations.

NF/mt