

New Mexico Legislature Revenue  
Stabilization Committee

# COMPARING NEW MEXICO'S TAX STRUCTURE TO OTHER STATES

JULY 6, 2022



# TAX POLICY PRINCIPLES

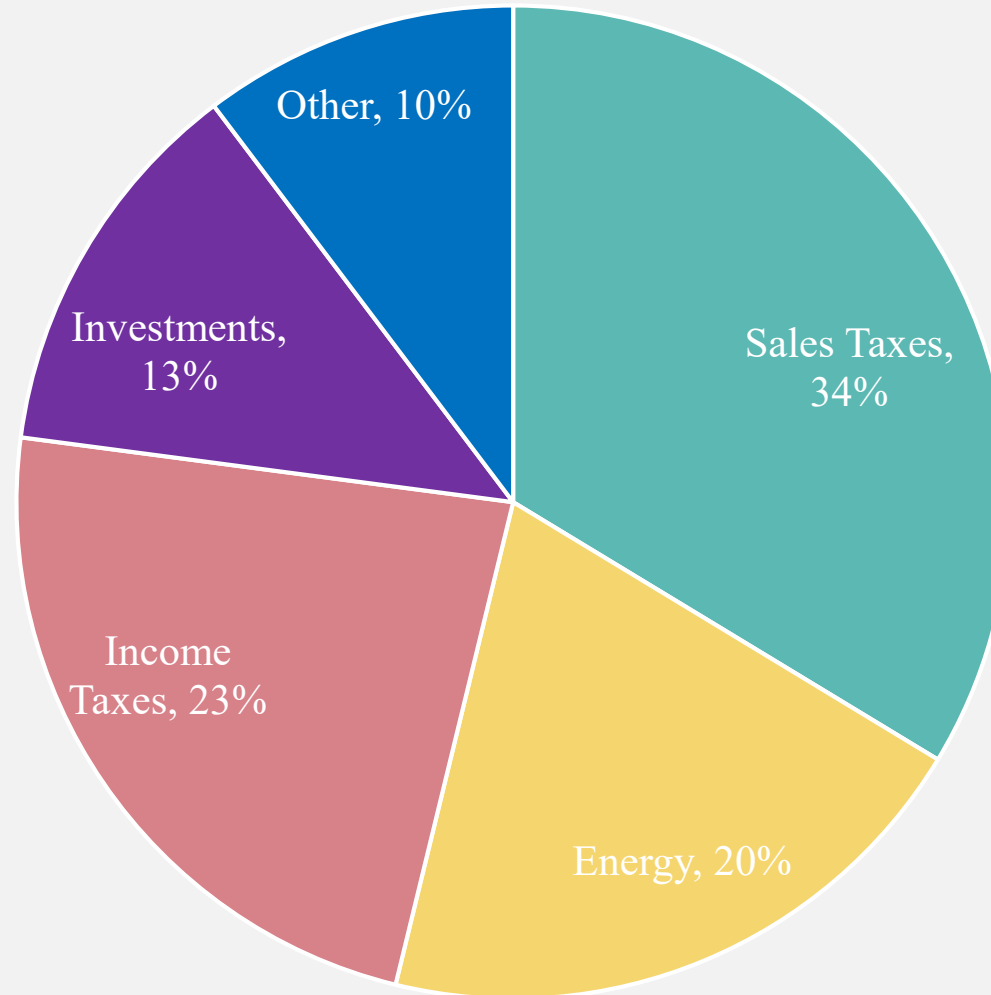
*N.M. Tax Research Institute is a non-profit, non-partisan member-supported organization dedicated to advancing the following principles of good tax policy in New Mexico:*

- ***Adequacy***
  - Revenues should be sufficient to fund needed services
- ***Efficiency***
  - Interference with the private economy should be minimized
- ***Equity***
  - Taxpayers should be treated fairly
- ***Simplicity***
  - Laws, regulations, forms and procedures should be as simple as possible
- ***Comprehensiveness***
  - All taxes should be considered when evaluating the system
- ***Accountability***
  - Exceptions should be rare and should be carefully evaluated and justified



# NEW MEXICO FISCAL SITUATION

General Fund 2023 Revenue: \$9.05B



## SALES TAX TREND – EXPANDING THE TAX BASE

- Multistate Tax Commission (MTC) – project studying how best to tax digital goods and services – following the approach of Washington, New Mexico, Hawaii and South Dakota – including those products generally and then providing general deductions (similar to tangible goods).
- Streamlined Sales and Use Tax States – project studying how to source digital goods and services for determining the local tax rate. The project recently dropped the idea of defaulting back to origin sourcing and will, instead, explore a one-rate default which the state will then distribute.



## SALES TAX TREND – EXPANDING THE TAX BASE

- New Jersey legislature asked the revenue department, along with Rutgers University, to study how the state's tax system treated the digital economy and how to best include digital products.
- Other states are beginning to consider expanding the sales tax base and cutting income tax rates.
- NOTE – the federal Internet Tax Freedom Act allows digital goods and services to be taxed if similar non-digital items are also taxed.



## PASS-THROUGH ENTITY TAXES

- Almost all states that have a “true” income tax impose the tax on partnerships and S corporations by computing the taxable income at the entity level and then imposing tax at the owner level.
- A handful of states including Texas, Ohio, Nevada, Washington, and DC have moved to a gross income or a margin tax imposed at the entity level for all businesses.
- The partnership income tax system is one of the most complicated areas of all tax law.



## PASS-THROUGH ENTITY TAXES

- Income reported in pass-through entities continues to far out-strip income reported in C-corporations.
- In part, this is due to the rise of venture capital, hedge funds, and private equity as a means to finance businesses through private ownership investment, rather than through public markets or borrowing.
- Last year, according to the Federation of Tax Administrators and other sources, almost all states with income taxes had much higher than expected revenues which are likely due to capital gains from these private investments in pass-through businesses.



## PASS-THROUGH ENTITY TAXES

- In 2017, Congress enacted the Tax Cuts and Jobs Act (TCJA), which among other things, capped the state and local tax deduction.
- This means residents in states with relatively high income taxes will pay more in federal tax than they otherwise would have.
- States began to pose an in-lieu of tax, called a “PTE tax” shortly after that would be paid at the partnership level—giving partners a credit against their own individual tax due.
- Now 27 states, including New Mexico, have such taxes.





## PASS-THROUGH ENTITY TAXES

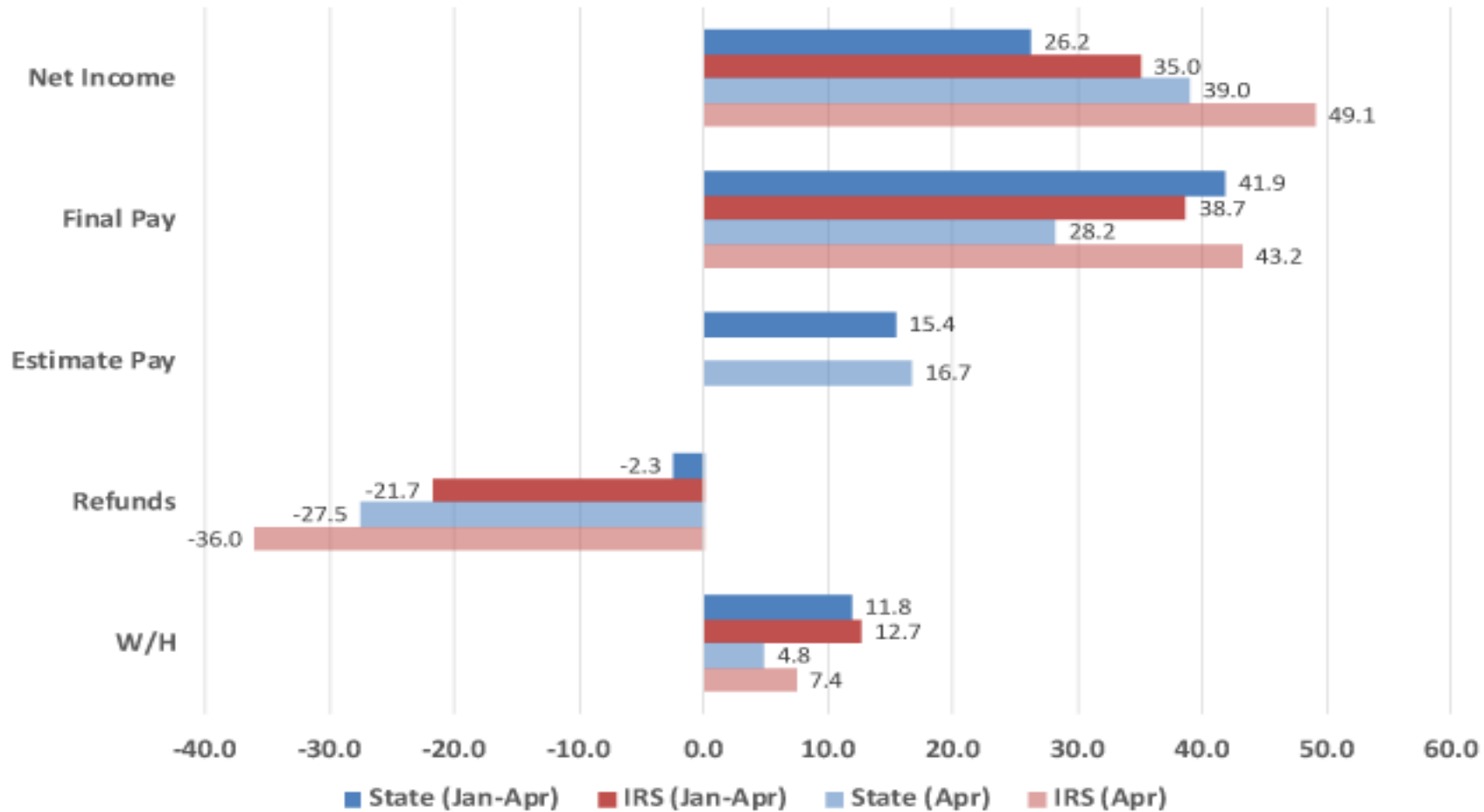
- Imposing a tax on partnership income at the entity level would be much simpler and much less prone to abuse than the pass-through system.
- This can be done without multiplying the tax or having it imposed twice—as the state PTE taxes have proven.
- The other issue is how to tax gains from sales of businesses. The federal government, in the TCJA, also passed a provision to tax foreign investors on gains from sales of partnerships doing business in the U.S. States are looking at doing something similar.
- The MTC also has a project looking at taxation of partnerships.



# ALL STATE FISCAL STATUS

State & Federal Individual Income Tax Collection - 2022 Processing Year

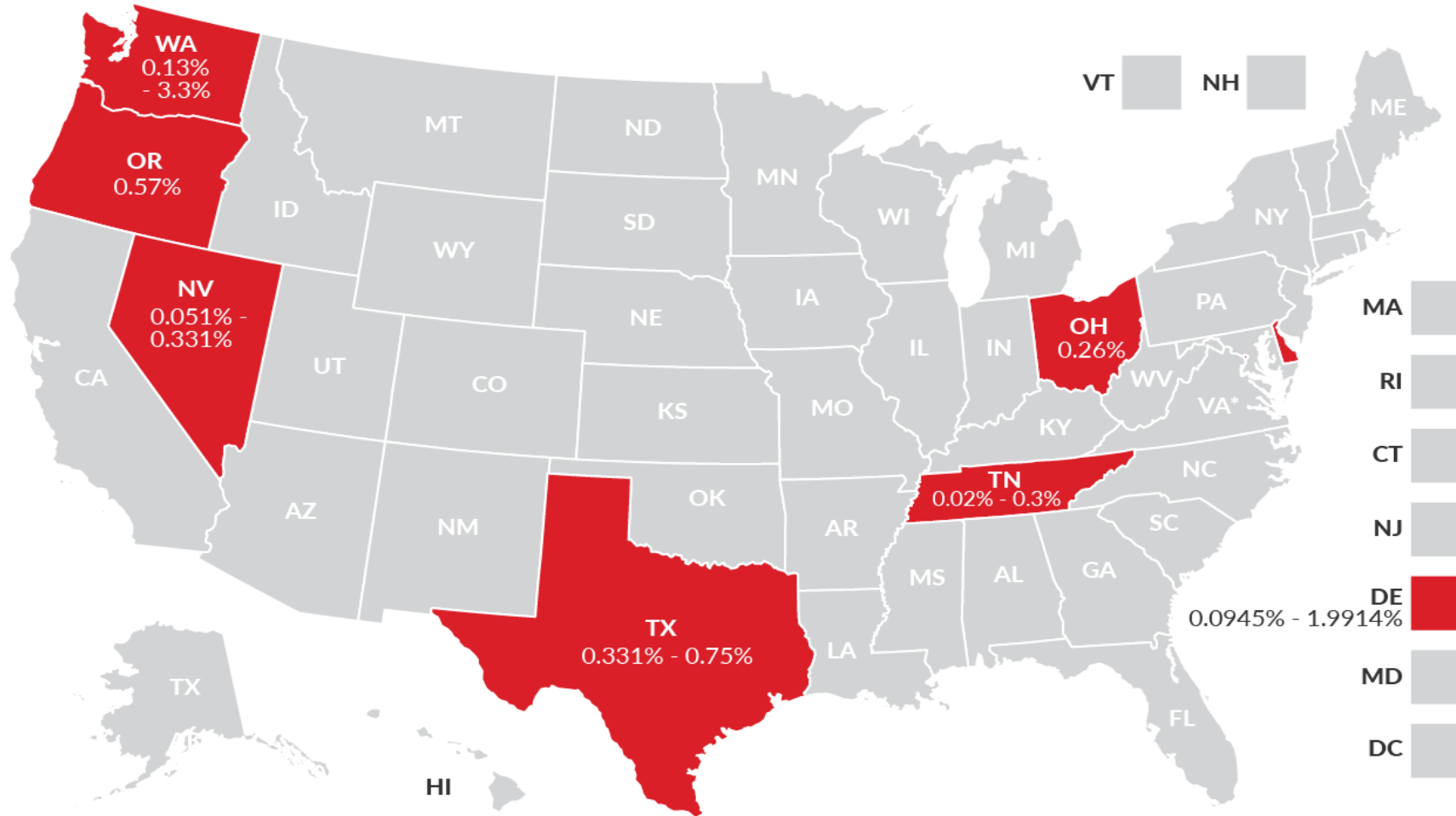
[percentage change - adjusted base]



Federation of Tax Administrators

# Does Your State Have a Gross Receipts Tax?

State Gross Receipts Taxes, January 2022



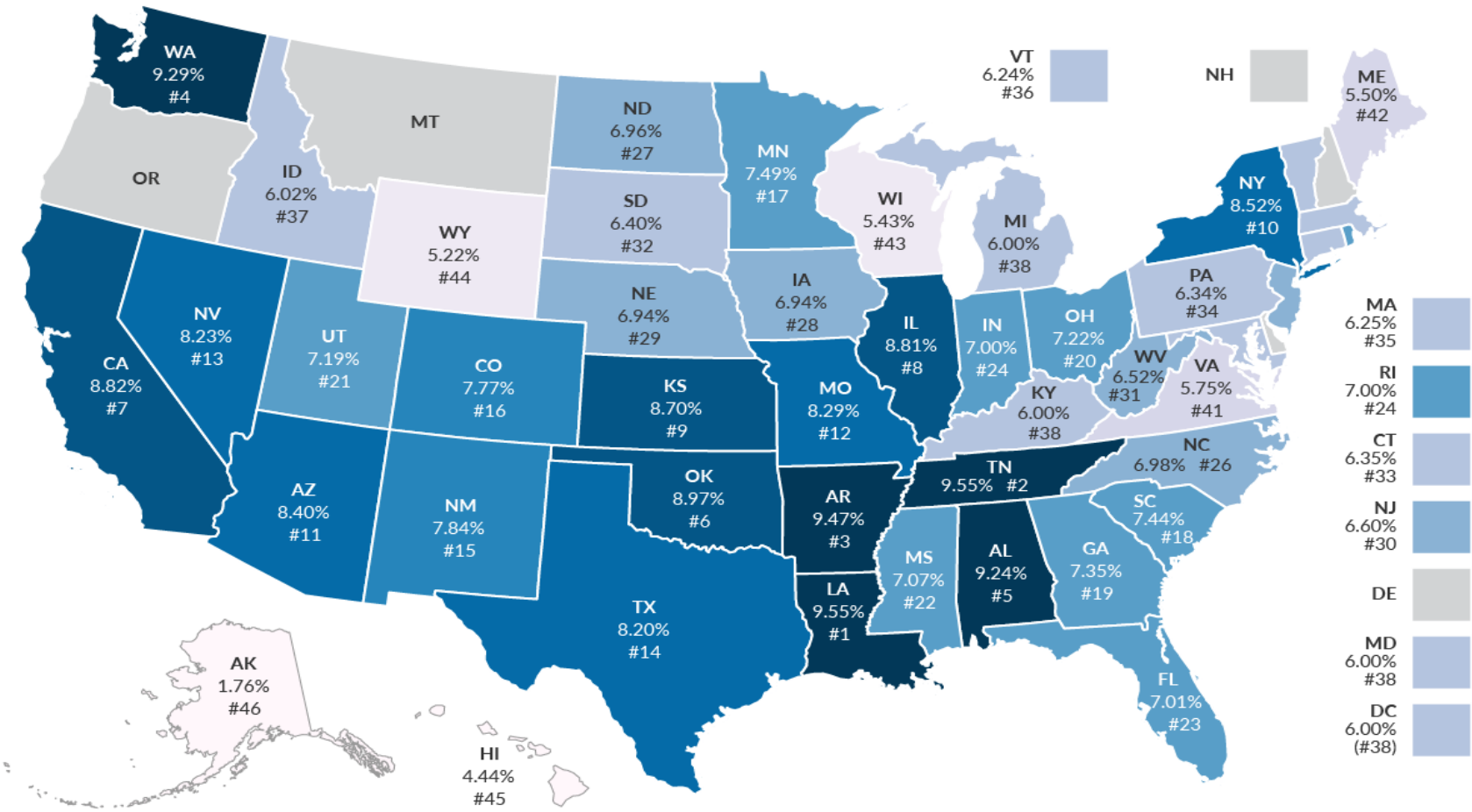
*State with gross receipts taxes*

\*Virginia's tax is locally levied and rates vary by business and jurisdiction. Approximately half of counties do not levy the tax. Some counties instead levy a capital stock tax.  
 Note: Gross receipts taxes are complex business taxes imposed at a low rate but on a wide base of transactions, resulting in high effective tax rates that can vary by industry. These taxes also often have minimum taxes that can result in much higher effective rates for some small businesses.  
 Source: Bloomberg Tax; state revenue departments; Weldon Cooper Center for Public Service.

■ Has a State Gross Receipts Tax  
■ No State Gross Receipts Tax

# How High are Sales Taxes in Your State?

Combined State & Average Local Sales Tax Rates, January 2022



*Combined Average State and Average Local Sales Tax Rates*

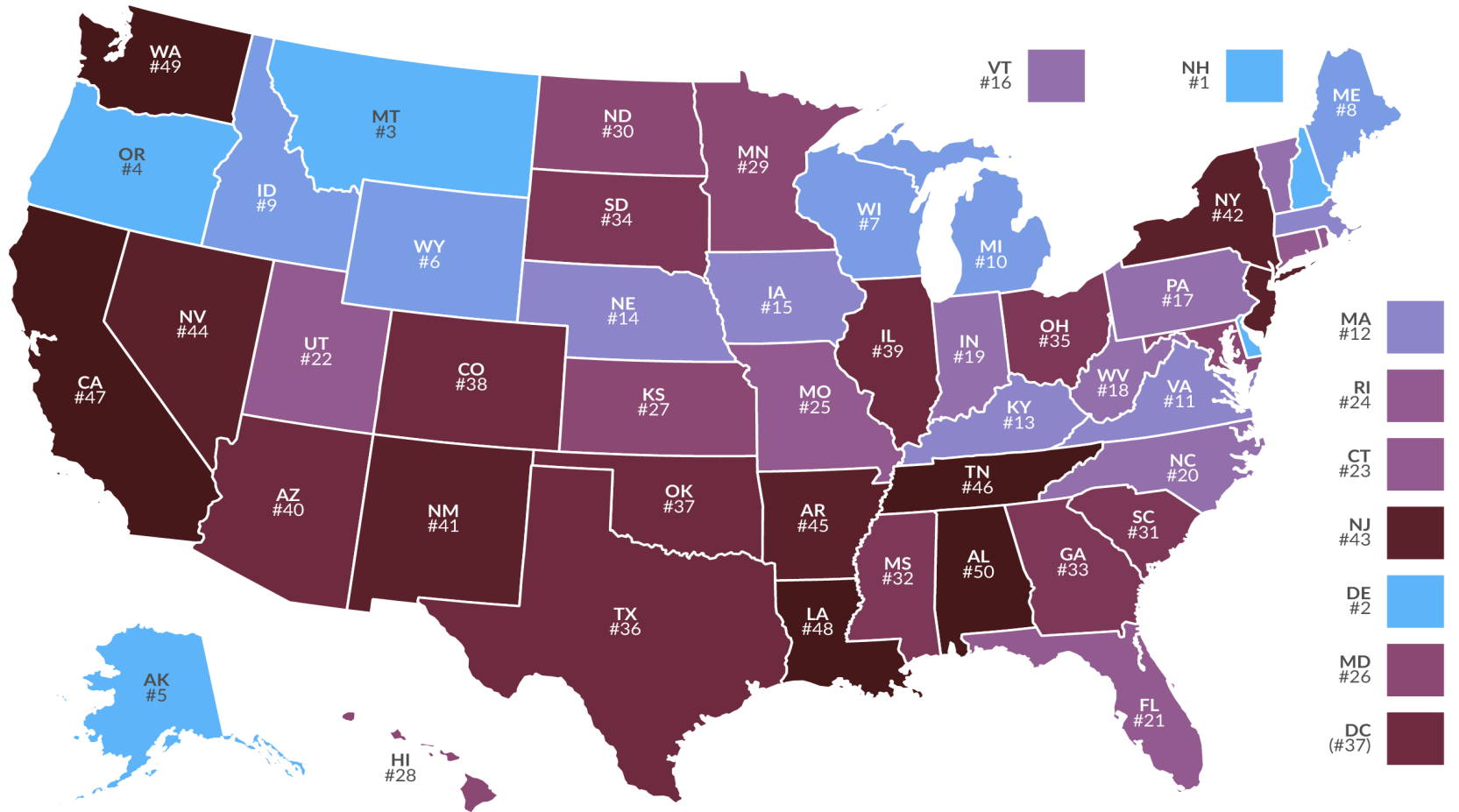
Notes: City, county and municipal rates vary. These rates are weighted by population to compute an average local tax rate. The sales taxes in Hawaii, New Mexico and South Dakota have broad bases that include many business-to-business services. D.C.'s rank does not affect states' ranks, but the figure in parentheses indicates where it would rank if included.

Sources: Sales Tax Clearinghouse; Tax Foundation calculations; State Revenue Department websites



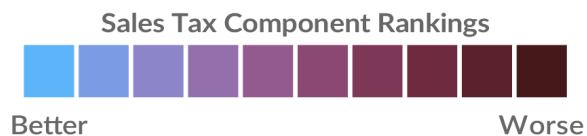
# How Does Your State Rank on Sales Taxes?

Sales Tax Component Rankings, 2022 State Business Tax Climate Index



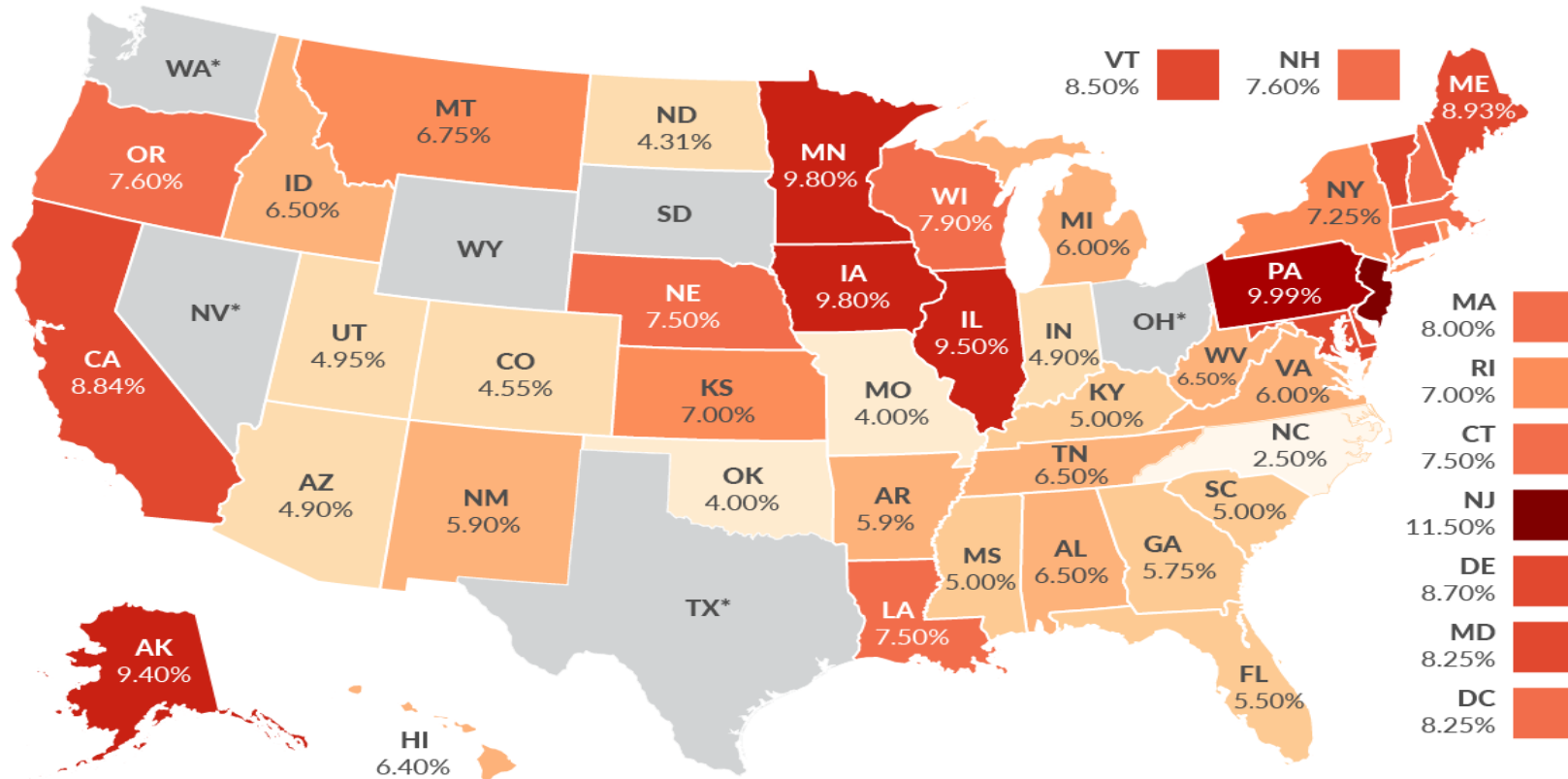
*TF Sales Tax Rankings*

Note: A rank of 1 is best, 50 is worst. D.C.'s score and rank do not affect other states. The report shows tax systems as of July 1, 2021 (the beginning of Fiscal Year 2022). Source: Tax Foundation, 2022 State Business Tax Climate Index.



# How High are Corporate Income Tax Rates in Your State?

Top State Marginal Corporate Income Tax Rates as of January 1, 2022



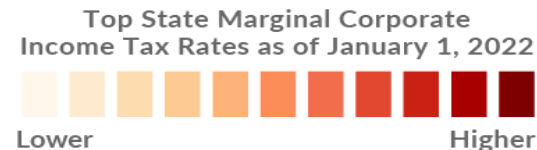
Note: In addition to regular income taxes, many states impose other taxes on corporations such as gross receipts taxes and franchise taxes. Some states also impose an alternative minimum tax and special rates on financial institutions.

\*Nevada, Ohio, Texas, and Washington do not have a corporate income tax but do have a gross receipts tax with rates not strictly comparable to corporate income tax rates. Delaware and Oregon have gross receipts taxes in addition to corporate income taxes, as do several states like Pennsylvania, Virginia, and West Virginia, which permit gross receipts taxes at the local (but not state) level.

Connecticut charges a 10% surtax on a business's tax liability if it has gross proceeds of \$100 million or more, or if it files as part of a combined unitary group. This surtax was recently extended and is scheduled to expire on January 1, 2023.

Illinois' rate includes two separate corporate income taxes, one at a 7% rate and one at a 2.5% rate. In New Jersey, the rates indicated apply to a corporation's entire net income rather than just income over the threshold. A temporary and retroactive surcharge is in effect from 2020 to 2023, bringing the rate to 11.5% for businesses with income over \$1 million.

Sources: Tax Foundation; state tax statutes, forms, and instructions; Bloomberg Tax.

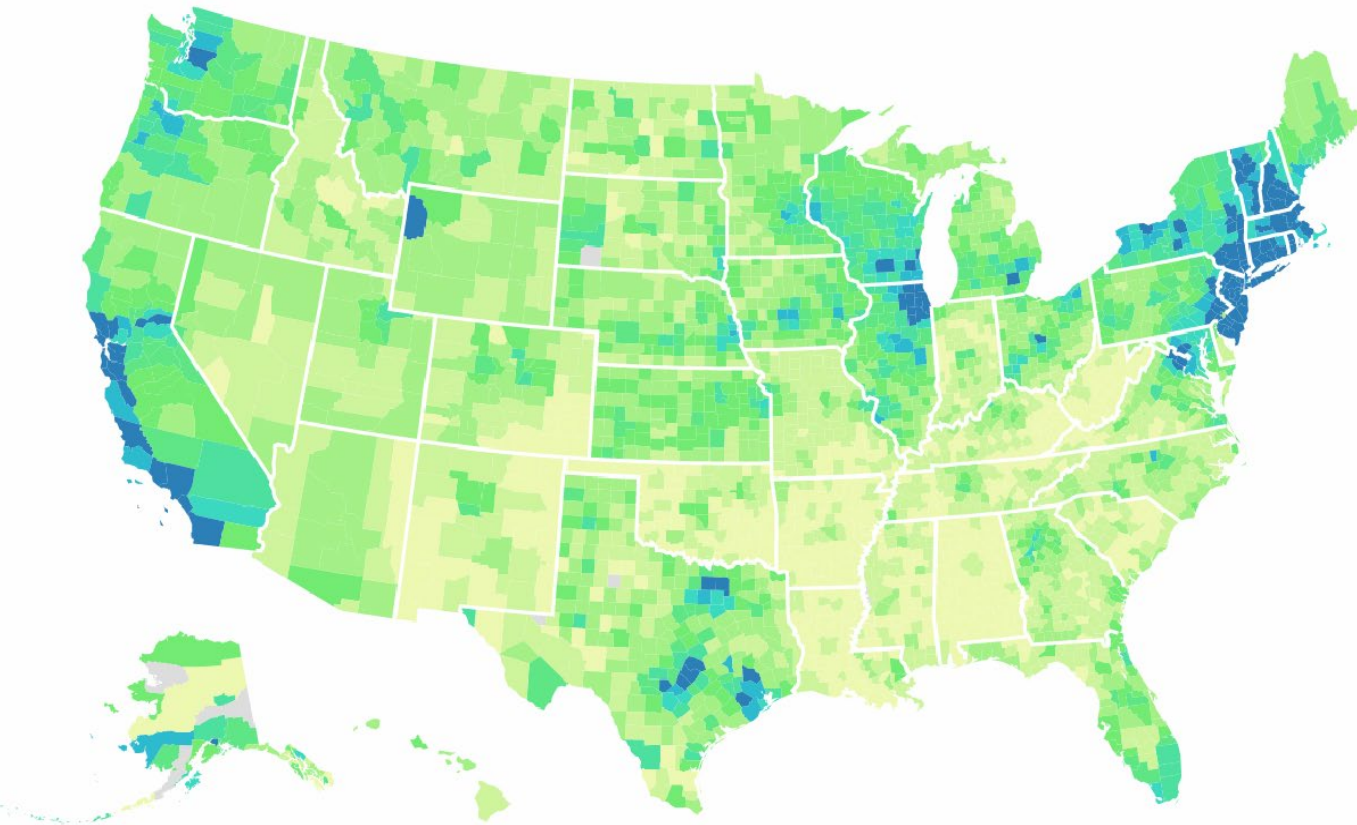


*Corporate Income Tax -  
Top Marginal Tax Rates*



# Where Do People Pay the Most in Property Taxes?

Median Property Taxes Paid by County, 2019 (5-year Estimate)



Median Property Taxes Paid by County, 2019 (5-year Estimate)



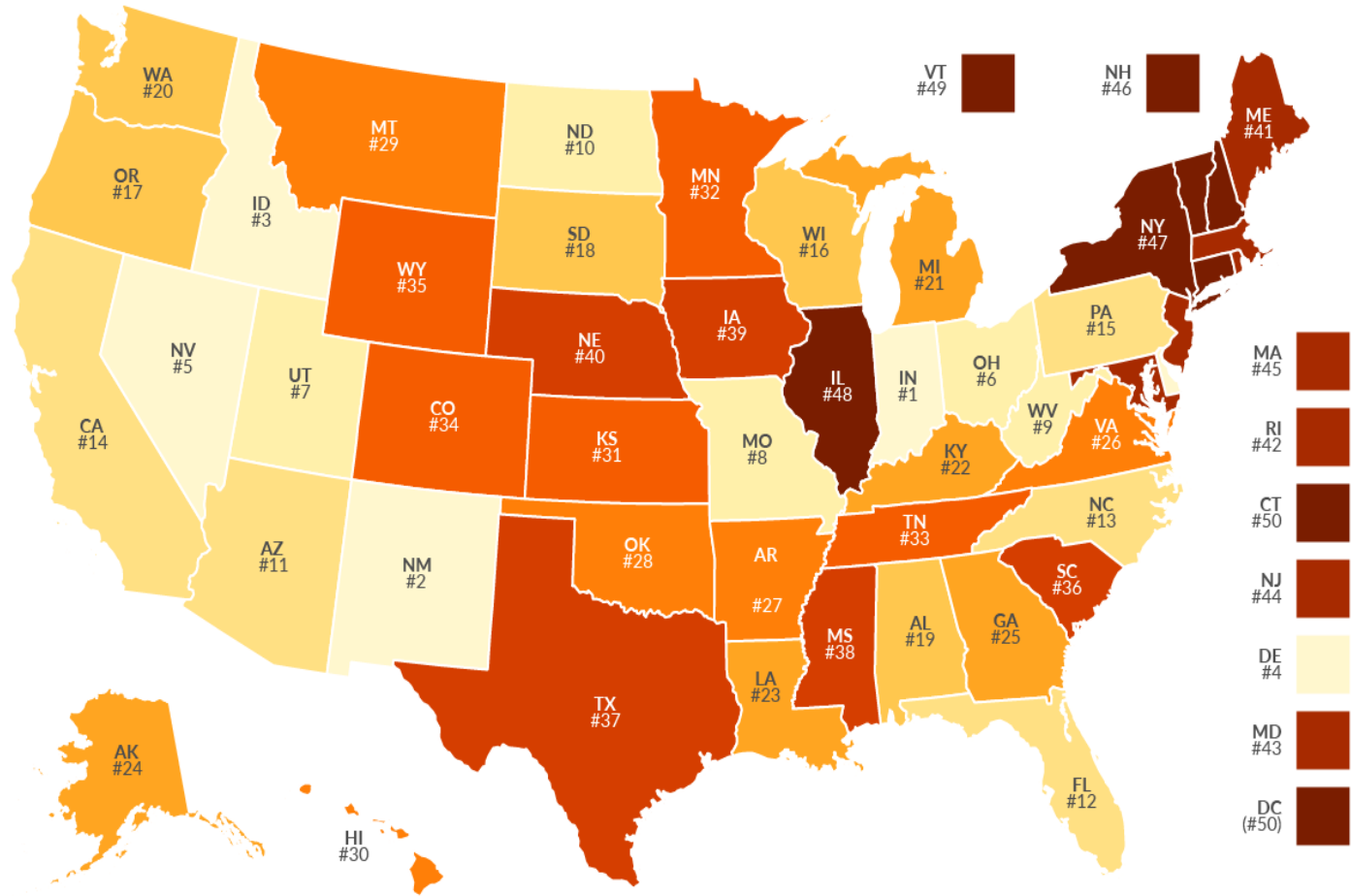
Note: Missing values are due to small sample sizes in low-population counties.  
Source: U.S. Census Bureau, 2019 American Community Survey dataset B25103.

*Property Tax – Median Tax Paid*



# How Does Your State Rank on Property Taxes?

Property Tax Component Rankings, 2022 State Business Tax Climate Index



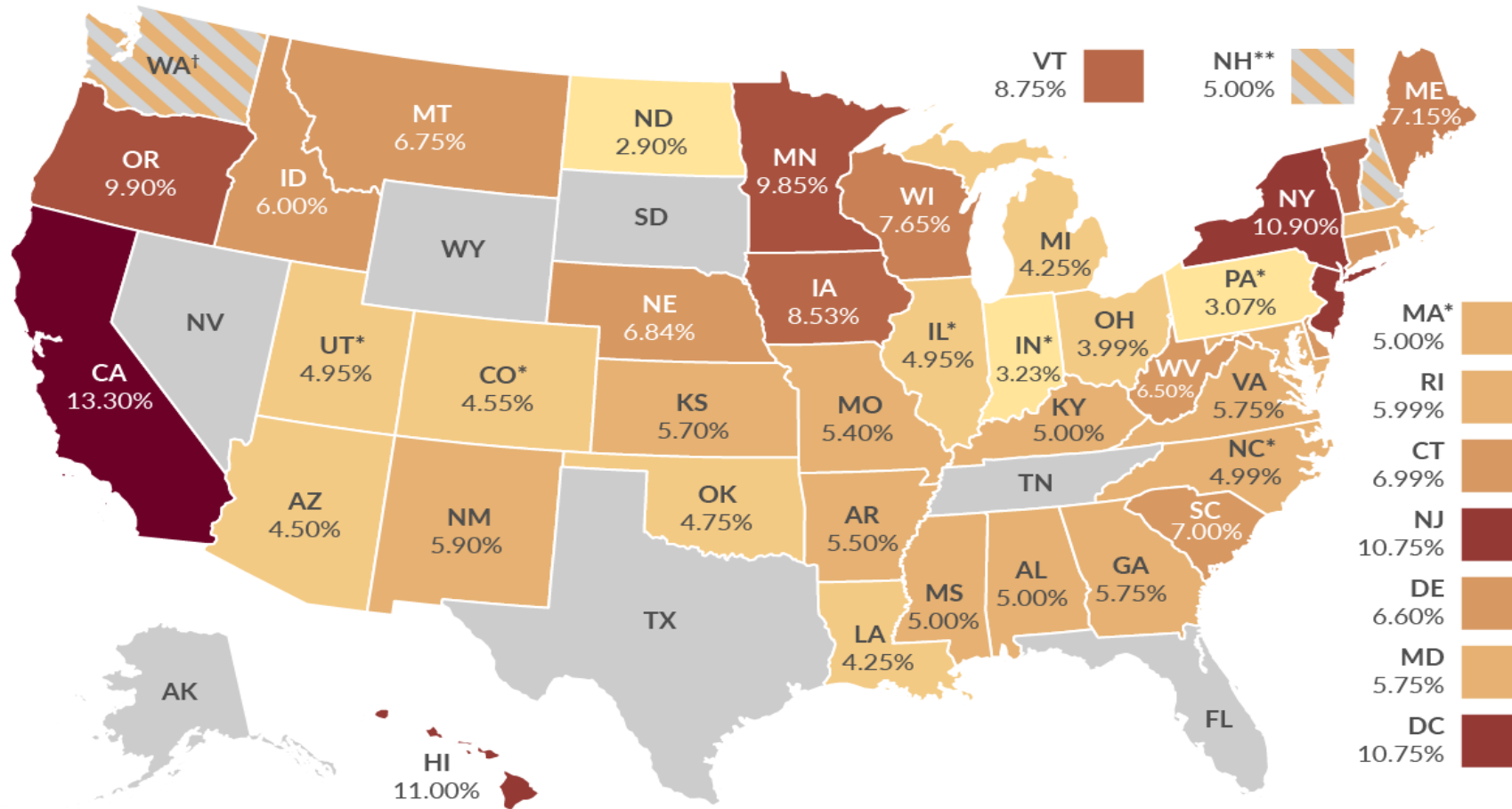
*TF Property Tax Rankings*

Note: A rank of 1 is best, 50 is worst. D.C.'s score and rank do not affect other states. The report shows tax systems as of July 1, 2021 (the beginning of Fiscal Year 2022).  
Source: Tax Foundation, 2022 State Business Tax Climate Index.



# How High Are Individual Income Tax Rates in Your State?

Top Marginal State Individual Income Tax Rates (as of January 1, 2022)



Note: Map shows top marginal rates: the maximum statutory rate in each state. This map does not show effective marginal tax rates, which would include the effects of phase-outs of various tax preferences. Local income taxes are not included. Missouri's top marginal rate will be reduced to 5.3% if certain revenue triggers are met.

(\*) State has a flat income tax.

(\*\*) State only taxes interest and dividends income.

(†) State only taxes capital gains income.

Sources: Tax Foundation; state tax statutes, forms, and instructions; Bloomberg Tax.

*Personal Income Tax -  
Top Marginal Tax Rates*

Top State Marginal Individual Income Tax Rates

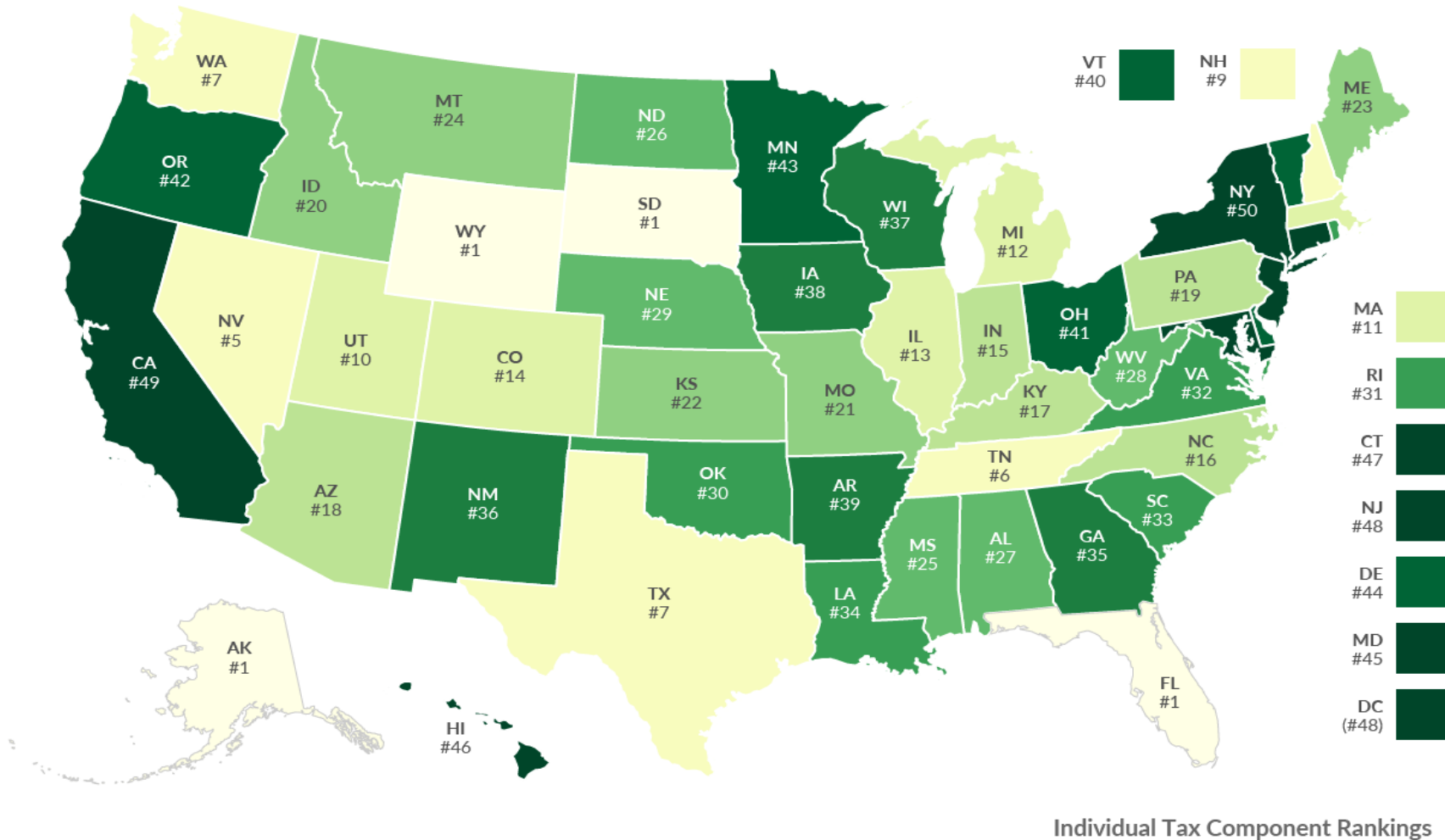


Lower

Higher

# How Does Your State Rank on Individual Income Taxes?

Individual Tax Component Rankings, 2022 State Business Tax Climate Index

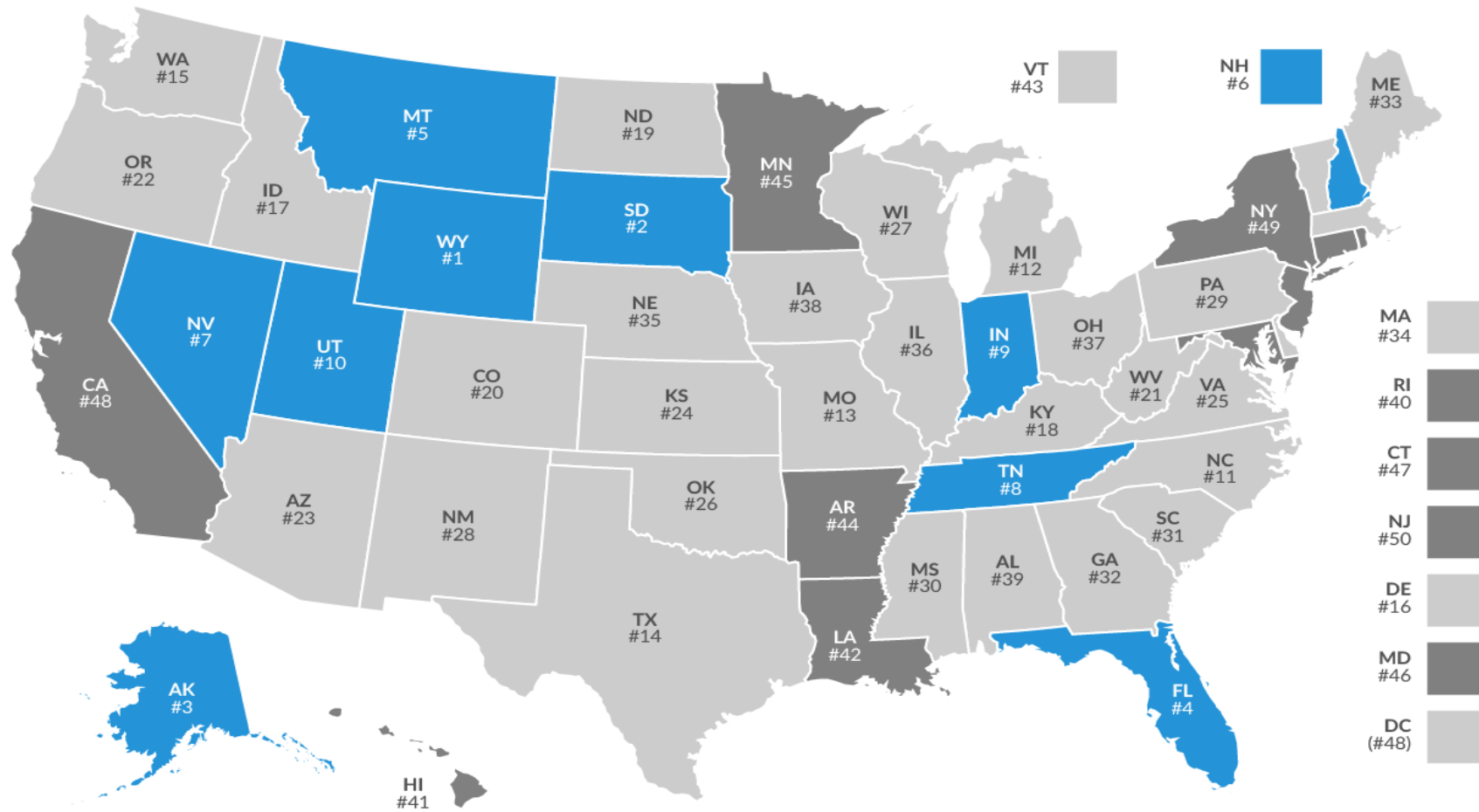


*Personal Income Tax –  
TF Rankings*

Note: A rank of 1 is best, 50 is worst. States without a corporate tax rank equally as 1. D.C.'s score and rank do not affect other states. The report shows tax systems as of July 1, 2021 (the beginning of Fiscal Year 2022).

Source: Tax Foundation, 2022 State Business Tax Climate Index.

# 2022 State Business Tax Climate Index



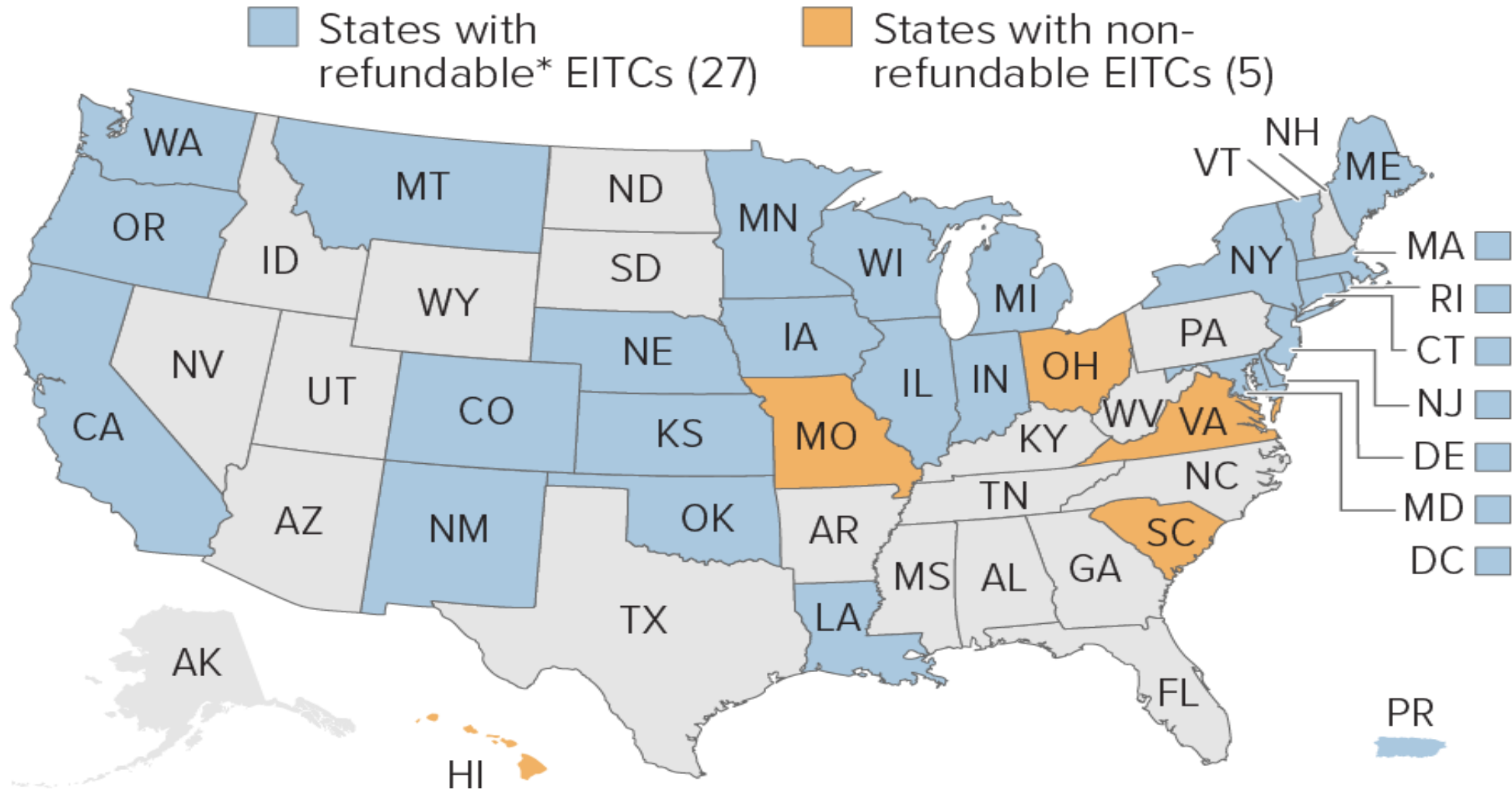
Note: A rank of 1 is best, 50 is worst. D.C.'s score and rank do not affect other states. The report shows tax systems as of July 1, 2021 (the beginning of Fiscal Year 2022).

Source: Tax Foundation

- 10 Best Business Tax Climates
- 10 Worst Business Tax Climates

*Tax Foundation  
Business Tax Climate  
Index Rankings*

# 30 States Plus D.C. and Puerto Rico Have EITCs



\*Refundability means that the full value of an earned income tax credit (EITC) is available to all families, no matter how much they owe in taxes.

Source: CBPP analysis. Data are as of 2021

# From the Tax Policy Center Study on How Broad are State Tax Bases

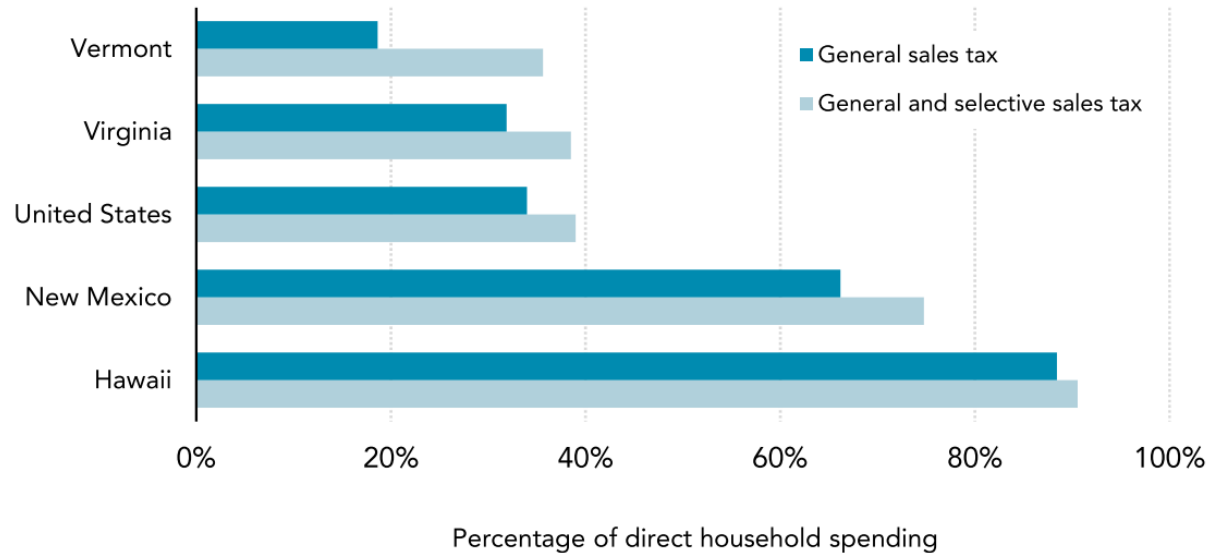
## SECTION 2: BREADTH OF SALES TAX BASE

### Most states include less than half of direct household spending in their sales tax base

- Using information about household spending patterns by state as well as state laws specifying the tax base for sales and excise taxes, we can determine the share of household direct spending that is taxable in each state.
- We measure direct household spending by subtracting expenditures by nonprofits and imputed expenditures from personal consumption expenditures.
- The share of the potential tax base covered by state general sales tax ranges from 19 percent in Vermont to 66 percent in New Mexico and 88 percent in Hawaii. If we include both general and selective sales tax, coverage rises to 36 percent in Vermont and to 75 percent in New Mexico and 91 percent in Hawaii.

FIGURE 4

### Sales Tax Base as a Percentage of Direct Household Spending for Selected States and the US, 2018



**Source:** Bureau of Economic Analysis, Regional Accounts Table SAEXP1; Bureau of Economic Analysis, National Income and Product Accounts Table 2.4.5U; and Bloomberg Sales and Excise Tax Navigators.

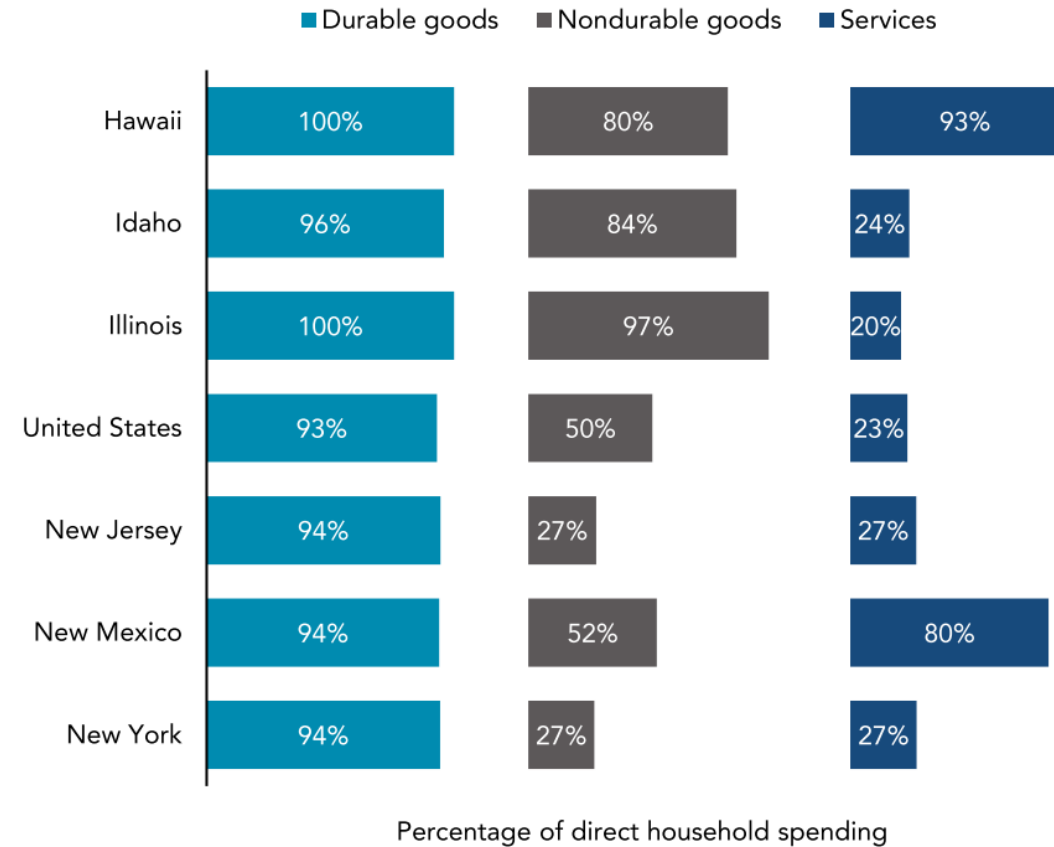
**Note:** Direct household spending is measured as personal consumption expenditures less final expenditures by nonprofits serving households and imputed items such as the rental equivalent of owned homes and financial services furnished without payment.

## Most states tax nearly all durable goods, but few tax a significant portion of services

- Almost all expenditures on durables are taxable in most states with a general sales tax. In some states, motor vehicle sales are exempt from general sales tax but are subject to a separate tax.
- Taxation of nondurable goods is far less uniform. Among states with a general sales tax, the percentage of nondurables subject to either the general sales tax or a separate tax ranges from 27 percent in New Jersey and New York to 84 percent in Idaho and 97 percent in Illinois. Three of the largest subcategories of non-durable goods—food at home, prescription drugs, and gasoline—are widely excluded from state general sales taxes, although all states levy a separate excise tax on gasoline.
- The percentage of service expenditures that is taxable ranges from 20 percent or less in many states to 80 percent in New Mexico and 93 percent in Hawaii.
- Alaska, Delaware, Montana, New Hampshire, and Oregon have no statewide general sales tax. However, all tax a small percentage of nondurable goods and (except for Alaska) some services through excise taxes.

FIGURE 5

## Tax Base Coverage by Expenditure Category, 2018




**Source:** Bureau of Economic Analysis, Regional Accounts Table SAEXP1; Bureau of Economic Analysis, National Income and Product Accounts Table 2.4.5U; and Bloomberg Sales and Excise Tax Navigators

**Note:** Direct household spending is measured as personal consumption expenditures less final expenditures by nonprofits serving households and imputed items such as the rental equivalent of owned homes and financial services furnished without payment.

# THANK YOU

Richard L Anklam  505 269 6791

 [Richard.Anklam@nmtri.org](mailto:Richard.Anklam@nmtri.org)

 [www.nmtri.org](http://www.nmtri.org)