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FISCAL IMPACT REPORT

SPONSOR Garcia, M.P. **ORIGINAL DATE** 02/09/10
LAST UPDATED _____ **HB** 245
SHORT TITLE Return Capital Gains Tax to Pre-2003 Rates **SB** _____
ANALYST Clifford

REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Non-Rec	Fund Affected
FY10	FY11	FY12		
\$19,000.0	\$45,640.0	\$61,600.0	Recurring	General Fund

(Parenthesis () Indicate Revenue Decreases)

SOURCES OF INFORMATION

LFC Files

Responses Received From

Taxation and Revenue Department (TRD)

SUMMARY

Synopsis of Bill

House Bill 245 would repeal the income tax deduction for up to 50 percent of net capital gains.

Provisions apply to tax years beginning on or after January 1, 2010.

FISCAL IMPLICATIONS

Fiscal impacts are uncertain. The latest year for which the state has information on capital gains reported by New Mexico taxpayers is 2007, and the amounts have certainly fallen significantly since that time.

SIGNIFICANT ISSUES

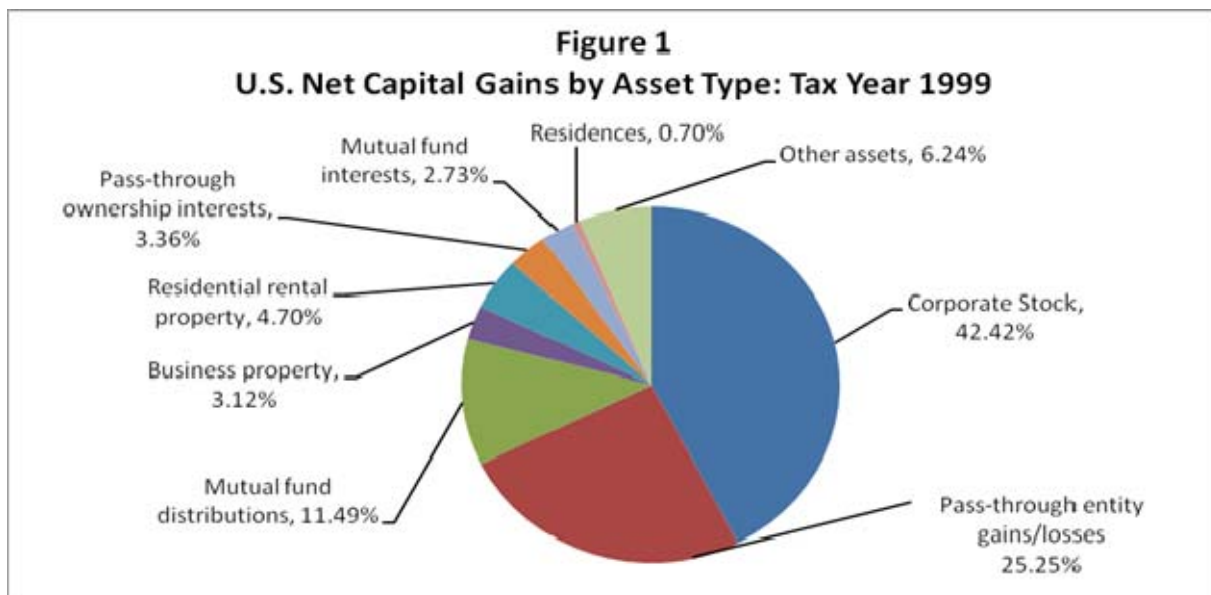
Since state income taxes are deductible by taxpayers who itemize deductions on their federal tax return, the net impact of the proposal on such taxpayers will be reduced by their effective federal tax rate.

The Blue Ribbon Tax Reform Commission recommended eliminating the capital gains deduction for high-income households. They also recommended providing a full deduction for gains on the sale of a closely-held business.

TRD:

Capital gains are primarily reported by higher income taxpayers, so reducing the capital gains deduction increases the portion of personal income tax paid by higher-income taxpayers, making the income tax more progressive. New Mexico’s tax rate on capital gains is among the lowest of any state that imposes an income tax. Most capital gains are realized on intangibles and other non-New Mexico assets. Capital gains realizations can be very volatile, so the option would increase the volatility of personal income tax revenues. Some current residents with substantial gains on New Mexico assets could leave the State, and some high-income non-residents with substantial gains on stocks and other intangible assets could be discouraged from establishing residency in the State.

The following chart illustrates the distribution of net capital gains by type of asset from a study of 1999 tax returns by the I.R.S.



Source: I.R.S. “Sales of Capital Assets: 1999”.

Of states in the region imposing an income tax, California and Arizona do not provide tax preferences for capital gains whereas Oklahoma, Colorado, and Utah do. Those three states provide more limited relief than New Mexico.

OTHER SUBSTANTIVE ISSUES

TRD:

Most states tax capital gains in the same manner that income from other sources is taxed. However, as of early 2009, New Mexico and eight other states with an income tax (Arkansas, Hawaii, Montana, North Dakota, Rhode Island, South Carolina, Vermont, and Wisconsin) allow significant tax reductions for capital gains income... States without an income tax impose no tax on capital gains (or other forms of income).

TRD provided the following table showing the distribution of the tax increase by gross income.

**Distribution of Change in Tax Year 2010 Tax Liability
(2007 Income Levels)**

Adjusted Gross Income	Number of Affected Returns	Change in Tax Liability		
		Total (\$000)	Average	Percent Distribution
Under 30,000	1,619	77	47	0.2%
30,000 - 40,000	1,463	105	72	0.3%
40,000 - 50,000	2,294	215	94	0.6%
50,000 - 60,000	2,568	318	124	0.9%
60,000 - 75,000	4,199	648	154	1.8%
75,000 - 100,000	6,471	1,298	201	3.6%
100,000 - 200,000	14,646	4,922	336	13.5%
200,000 - 500,000	8,845	7,150	808	19.7%
500,000 or more	6,398	21,607	3,377	59.5%
Total	48,503	36,339	749	100.0%

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