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Report: State can boost opportunity, combat inequality by expanding taxes

A historically large share of the nation's wealth is concentrated in the hands of a few, reducing opportunities for millions of Americans and reinforcing barriers that make it harder for people of color to make gains.

These inequities are made worse by most state tax systems – including New Mexico's. By designing better tax policy, state lawmakers can help spread opportunity more widely and build more broadly shared prosperity.

Among the solutions on state policymakers' lists should be expanding the taxation of assets of the very wealthy, since loopholes and other special benefits currently shield much of the value of these assets from federal, state, and local taxes, a new series of reports by the Center on Budget and Policy Priorities argues.

Eliminating these tax advantages would shift some of the responsibility for funding critical public services and investments like schools, roads, and health care from low- and moderate-income taxpayers to those best able to pay, while increasing opportunity for everyone.

How States Can Tax Wealth , which launched Dec. 12 with two short Issue Briefs (listed below), explores how states can better tax wealth and high incomes to make state tax codes fairer, raise adequate funding for public services, and expand opportunity.

Issue Brief: State Taxes on Inherited Wealth : State taxes on inherited wealth apply only to the wealthiest individuals and are the primary state tax on wealth. But these taxes have gradually eroded, even as wealth and income have become more concentrated. States with these taxes should maintain them, and states without them should consider enacting them – or consider taxing inheritances as income. State taxes on inherited wealth are not affected by the federal estate tax. Reinstating an estate tax in New Mexico with a $1 million exemption would raise an estimated $40 million each year to fund education, health care, and other important public services.

Issue Brief: State Taxes on Capital Gains : Capital gains income, which goes overwhelmingly to the wealthiest households, receives special tax preferences in a number of states. In New Mexico, tax filers can deduct 50 percent of this unearned income from their state taxes, costing the state between $20 million and $55 million per year. States with such preferences should eliminate them.

“State policymakers across the country and across the political spectrum agree that inequality and the increasing concentration of wealth is a problem,” Elizabeth McNichol, Senior Fellow at CBPP and project lead on this new series, said. “The good news is there are plenty of policy solutions that can improve state tax systems, raise new revenues for important public investments, and boost opportunities for workers and families striving to get ahead. Our new series can help lawmakers make smarter decisions in 2019 and beyond.”

Nationwide, the top 1 percent of households own roughly 40 percent of the wealth, while the bottom 90 percent of households own just 21 percent.

This top-heavy structure reduces opportunity for millions of American families – particularly black families, Hispanic families and other families of color, who have faced additional barriers to building wealth due to the legacy of historical racism and the ongoing damage from racial bias and discrimination.

In New Mexico, the median net worth of white households is nearly ten times that of households of color.

This staggering inequity is especially concerning in New Mexico, where people of color make up the majority of the population.

State and local governments largely exacerbate this disparity through the state and local tax code, which asks low- and middle-income taxpayers in most states to pay a larger share of their income in taxes than the wealthiest taxpayers.

In New Mexico, the lowest-income 20 percent of taxpayers face an average state and local tax rate that’s almost double what the top 1 percent of households pay. The average effective state and local tax rate is 10.6 percent for the lowest-income 20 percent of individuals and families, 10.2 percent for middle 20 percent, and 6 percent for the top 1 percent.

Over the past 15 years in New Mexico, more than $1 billion a year has been handed out via income tax cuts that mostly benefited those with the highest incomes and out-of-state corporations.

That huge loss of revenue, in turn, has led to big budget cuts, particularly in K-12 and higher education – two areas that need robust investments for states to have strong economies.

New Mexico Voices for Children, which is partnering with CBPP on the report release, is calling for tax policies that are both fairer and that bring in adequate revenue. Among those policies are repealing the deduction for capital gains income and raising the tax rate on the highest incomes.

“Better tax policies like these are an important tool for creating a state with more opportunity and more broadly shared prosperity,” James Jimenez, executive director of NM Voices, said. “Improving and expanding the taxation of wealth could help bring more balance to our state’s tax code by ensuring the wealthiest families are paying their share toward building a stronger New Mexico.”

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