LEGISLATIVE EDUCATION STUDY COMMITTEE
BILL ANALYSIS

Bill Number: SB 13 **51st Legislature, 1st Session, 2013**

Tracking Number: .190366.2

Short Title: Corporate Income Tax Rates & Reporting

Sponsor(s): Senator Peter Wirth

Analyst: Ian Kleats **Date: February 15, 2013**

Bill Summary:

SB 13 amends sections of the *Corporate Income and Franchise Tax Act* to lower all marginal corporate income tax rates by 0.6 percent:

- to 4.2 percent from 4.8 percent for income under $500,000;
- to 5.8 percent from 6.4 percent for income between $500,000 and $1,000,000; and
- to 7.0 percent from 7.6 percent for income greater than $1,000,000.

SB 13 also amends sections of the *Corporate Income and Franchise Tax Act* to provide for mandatory combined reporting of unitary corporations for tax purposes.

The bill specifies an effective date for the bill's provisions of January 1, 2014, and the provisions would be applicable to taxable years beginning on or after January 1, 2014.

Fiscal Impact:

SB 13 does not contain an appropriation.

Estimated Revenue Impact*				R or NR**	Fund(s) Affected
FY 13	FY 14	FY 15	FY 16		
0	890	(960)	(9,140)	R	General Fund

* In thousands of dollars. Parentheses ( ) indicate a revenue loss.
** Recurring (R) or Non-Recurring (NR).

The estimate above comes from the Taxation and Revenue Department (TRD) bill analysis. TRD further estimates a negative revenue impact of almost $16.0 million for FY 17.

According to the TRD analysis:

- revenues from affected corporations are expected to increase by 10 percent initially due to the combined reporting changes;
- the rate of increase is expected to slow to 5.0 percent during the later years as taxpayers adjust their corporate structures and transactions to avoid taxation; and
- any revenue increases from mandatory combined reporting are offset by revenue decreases from the lower marginal tax rates beginning in FY 15.

TRD provided no explanation for the initial revenue increases, but it is the understanding of the LESC staff that the upfront revenue increase in TRD's estimate is due to the combined reporting changes becoming effective prior to the first corporate income returns being filed subject to the proposed lower rates. This would explain the sharp increase in revenue exposure occurring after FY 15.

Fiscal Issues:

Based on the estimated fiscal impact, the bill could reduce General Fund revenue by approximately $16.0 million at its peak in FY 17, with similar or greater revenue exposure occurring in years thereafter.

Based on *General Appropriation Act* appropriations for the last five years, the Legislature has appropriated approximately 43.5 percent of General Fund revenue for public education. The reduction of revenue from the General Fund as proposed in this bill could result in decreased annual appropriations of at least $6.96 million for public education in future fiscal years.

Technical Issues:

TRD notes that, although the *Corporate Income and Franchise Tax Act* defines "unitary" corporation, the definition contains a number of terms that are subject to varying interpretation. This point raises concerns for TRD that, if treatment of those issues is not clarified in statute, it could increase the possibility of litigation in the future.

Substantive Issues:

TRD suggests that "mandatory combined reporting may discourage corporations with profitable operations in other states from locating in New Mexico, since profits from existing operations would be partially taxable in New Mexico even though their New Mexico start-up operation was not profitable."

Background:

According to TRD, all other Western states with a corporate income tax mandate combined reporting of unitary corporations, but some of those states have additional provisions for single sales factor apportionment of income, which can be more advantageous for corporations than the three-factor (payroll, property, and sales) apportionment currently employed in New Mexico. The Blue Ribbon Tax Commission[1] endorsed the concept of mandatory combined reporting in 2003, although the commission recommended that the added revenue from combined reporting be used to reduce the corporate income tax rate.

Committee Referrals:

SCORC/SFC

[1] The Blue Ribbon Tax Reform Commission was created by Laws 2003, Chapter 77 to deal with a widespread feeling that New Mexico's tax system no longer fully meets the state's diverse needs. A complete record of the Commission's work can be found at: http://www.nmlegis.gov/lcs/bluetaxcomm.aspx

<u>Related Bills</u>:

SB 59 *Corp. Tax, Reporting, Single Sales & Repeals*
SB 277 *Single Sales & Reduce Corporate Sales Tax*
SB 368 *Reform Tax Code*
*SB 538 *Corporate Tax & Manufacturing*
HB 369 *Reform Tax Code*