LEGISLATIVE EDUCATION STUDY COMMITTEE
BILL ANALYSIS

Bill Number: **SB 222** **51st Legislature, 2nd Session, 2014**

Tracking Number: **.196084.1**

Short Title: **Pre-K Provider Gross Receipts**

Sponsor(s): **Senator John Arthur Smith**

Analyst: **Ian Kleats** **Date:** **February 7, 2014**

Bill Summary:

Effective July 1, 2014, SB 222 enacts a new section of the *Gross Receipts and Compensating Tax Act* exempting from gross receipts tax (GRT) the receipts of for-profit pre-kindergarten providers who provide pre-kindergarten services under the *Pre-Kindergarten Act*.

Fiscal Impact:

SB 222 does not contain an appropriation.

Fiscal Issues:

The Children, Youth and Families Department (CYFD) bill analysis:

- estimates that, based on FY 14 appropriations, approximately $5.1 million went to for-profit pre-kindergarten providers; and
- indicates that exempting the receipts of for-profit providers from GRT would not change the overall allocation for those providers.

It is unclear whether the exemption would result in more funds being available for classroom instruction or create higher profits for the providers.

The Taxation and Revenue Department (TRD) bill analysis suggests that SB 222 could reduce General Fund and local government revenue by an average of $452,000 annually over the next four years. However, this estimate does not appear to consider receipts from services other than pre-kindergarten (see "Technical Issues," below).

Under current law, the receipts from non-profit pre-kindergarten providers that provide services pursuant to the *Pre-Kindergarten Act* are exempt from GRT. Any pre-kindergarten provider could structure as a non-profit, 501(c)(3) corporation to take advantage of the current exemption.

Technical Issues:

SB 222 would exempt all receipts of for-profit pre-kindergarten providers from GRT, even those receipts from services other than pre-kindergarten, such as daycare. The sponsor may wish to consider limiting exempted receipts to only those received from CYF for pre-kindergarten services.

Substantive Issues:

Under most instances, a GRT deduction could be considered preferable to a gross receipts tax exemption from a tax policy perspective because the use of deductions can be tracked to a greater degree than exemptions; current law does not provide for exempted receipts to be included on GRT returns.

One significant lesson learned from the *2013 New Mexico Tax Expenditure Report* is that data are necessary to gauge not only the revenue impact of deductions, but also the economic impact of those tax policies. Although reporting requirements impose an administrative burden on TRD and taxpayers, it could be considered a reasonable cost of receiving preferential treatment for tax purposes.

Economic Impact

Economic multiplier effects of any tax expenditure should be judged relative to multiplier effects from the likely use of the foregone government revenue. General Fund appropriations comprise many diverse uses with the largest proportion going to fund public education. Without strong evidence to the contrary, an assertion that this deduction has an economic multiplier higher than economic base jobs and expenditures associated with public education or any other governmental program might be considered speculative.

Moreover, New Mexico's State Equalization Guarantee education funding formula implies that over 40 percent of government revenue would be spread equitably across the state, impacting small rural communities in a proportionate level to larger urban communities. It is unclear whether this deduction could ensure the same equitable economic impact to all communities that public school funding would provide, even absent any discussion of the relative economic multiplier effects of the tax policy.

Background:

New Mexico *Pre-Kindergarten Act*:

- mandates that Pre-K programs prioritize serving at-risk communities;
- requires that any money appropriated for pre-kindergarten programs shall be divided equally between the Public Education Department (PED) and CYFD.
- creates two non-reverting funds:
    - ➢ Public Pre-Kindergarten Fund, administered by PED; and
    - ➢ Pre-Kindergarten Fund, administered by CYFD; and
- up to 10 percent of the money in each fund may be used for administrative expenses by the respective departments.

Committee Referrals:

SCC/SEC/SCORC/SFC

Related Bills:

HB 252 *Pre-K Provider Gross Receipts* (Identical)
HB 302 *Pre-K Provider Gross Receipts* (Identical)