F I S C A L   I M P A C T   R E P O R T

ORIGINAL DATE 3/7/19
SPONSOR Sharer **LAST UPDATED** **HB**

SHORT TITLE Tax Reform **SB** 358

ANALYST Clark

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY19	**FY20**	**FY21**	**FY22**	**FY23**		
	~($1,300,000.0)	~($2,700,000.0)	See Fiscal Implications		Recurring	General Fund
	Indeterminate	Indeterminate	Indeterminate	Indeterminate	Recurring	Local Governments

Parenthesis ( ) indicate revenue decreases

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY19	FY20	FY21	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
Total	Very Significant	Very Significant		Very Significant	Nonrecurring	TRD Operating Budget, Local Governments

Parenthesis ( ) indicate expenditure decreases

Conflicts with HB6, SB421, and nearly all other tax bills

SOURCES OF INFORMATION
LFC Files

NO Responses Received From
Taxation and Revenue Department (TRD)

Responses Received From
New Mexico Municipal League
Department of Transportation (NMDOT)
Human Services Department (HSD)
Higher Education Department (HED)

SUMMARY

Synopsis of Bill

Senate Bill 358 is a comprehensive, sweeping tax reform bill that eliminates most gross receipts tax (GRT) exemptions, deductions, and credits, significantly broadening the tax base; lowers the GRT rates for the state and local governments; and repeals the personal and corporate income taxes, instead taxing income through the GRT. The bill also repeals the motor vehicle excise tax, placing motor vehicles under GRT. In short, it turns the state's current hybrid of a pure GRT and a conventional sales tax into a true GRT or turnover tax. Below is a list of some key actions:

- Reduce state GRT rate from 5.125 percent to 1 percent;
- Reduce GGRT rate from 5 percent to 1 percent;
- Reduce municipal and county GRT rates to 0.5 percent maximum each and remove restrictions for use of funds for individual increments;
- Reduce the compensating tax rate;
- Repeal all provisions of the income tax and corporate income tax (except for 7-2A-29 NMSA 1978 – an apparent technical error);
- Subject wages and salaries to the GRT;
- Require the Taxation and Revenue Department (TRD) to adjust the GRT rate for three years (impacting FY21-FY23) to set projected revenue within a specified percentage range above the prior fiscal year's budget;
- Repeal most exemptions;
- Repeal most deductions;
- Repeal most credits;
- Tax internet sales;
- Repeal the estate tax;
- Repeal the motor vehicle excise tax (MVEX) in favor of vehicles being taxed under the GRT;
- Repeal the leased vehicle GRT and treat these transactions as regular gross receipts tax transactions;
- Repeal the boat excise tax;
- Replace county obligations with state obligations for county-supported Medicaid and safety net care pool;
- Provide temporary amnesty from penalties and interest; and
- Provide the repeal of certain taxes shall not impair outstanding bonds or loan guarantees.

The effective date of the provisions of the bill is January 1, 2020, except for the switch to destination sourcing for GRT, which becomes effective July 1, 2021.

FISCAL IMPLICATIONS

It is impossible to score precisely the fiscal impact of any significant tax reform bill, but it is particularly challenging to score a reform bill of this magnitude due to limitations in available data. Additionally, the significant number of interactive effects in this bill could have unanticipated consequences.

The GRT base broadening is significant, but it appears insufficient at the rates initially set in the bill (1 percent state rate and 0.5 percent rate each for municipalities and counties, for a total of 2 percent) to compensate state and local governments for revenue lost from the rate reduction and loss of other sources of revenue. The bill has a provision for TRD to reset the rates on July 1 of 2021, 2022, and 2023, although there are technical issues with this language. The intent appears to be for TRD to reset the rates to ensure revenue growth between 1.5 percent and 3 percent above the level of the prior fiscal year's budget.

It is impossible to estimate the impacts with any precision because of incomplete data on the value of many of the repealed exemptions and deductions and imprecise methods of estimating some other bill provisions. However, it appears the combined state plus local GRT rate would need to be about 3.9 percent (2.8 percent state-only) to achieve revenue neutrality.

Due to the rate reset provision and related technical issues with that provision, the fiscal impact table only shows estimates for FY20 and FY21 – general fund losses of about $1.3 billion and $2.7 billion, respectively.

If the technical issues were corrected, significant assumptions would still need to be made to estimate impacts in future fiscal years. Below is one possible method for this estimation.

> Assume rates for FY22 and FY23 are reset to equal the prior year budget plus 2.25 percent growth – halfway between the two ends of the given range. However, also assume that in FY20, the bill going into effect halfway through the year would eliminate the state's reserves and require budget cuts in that fiscal year followed by additional budget cuts in FY21 so that the FY21 budget would equal the FY20 budget (as initially set in the 2019 legislative session) reduced by the ratio of the rate set by the bill to the rate needed for neutrality. This leads to revenue growth in future years, but it is growth on top of a far smaller revenue base than projected by the consensus revenue estimating group under current law.

The New Mexico Department of Transportation (DOT) provided the following analysis.

Estimated Revenue				**Recurring or Non-Rec**	**Fund Affected**
FY20	**FY21**	**FY22**	**FY23**		
(3,365)	(6,890)	(7,040)	(7,170)	Recurring	State Road Fund (MVEX)
(77,750)	(159,200)	(162,500)	(165,600)	Recurring	General Fund (MVEX)
(3,255)	(6,560)	(6,540)	(6,510)	Recurring	Highway Infrastructure Fund (LVGRT)
(1,085)	(2,190)	(2,180)	(2,170)	Recurring	Local Governments Road Fund (LVGRT)
(585)	(1,220)	(1,280)	(1,290)	Recurring	Aviation Division (Jet Fuel)
(615)	(1,260)	0**	0**	Nonrecurring	Aviation Division (Air Assistance) **
Various***	Various***	Various***	Various***	Recurring	Numerous***

> The bill repeals the MVEX. Under current law, the State Road Fund receives 4.15% of the MVEX revenue (representing about $6.5-7 million per fiscal year), while the remaining amount (95.85%) is distributed to the General Fund.

> The bill also repeals the LVGRT, 75% of which is distributed to the Highway Infrastructure Fund and 25% of which is distributed to the Local Governments Road Fund. The LVGRT accounts for more than three quarters of the current revenues in Highway Infrastructure Fund.
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> Further, it eliminates certain revenue distributions to the Aviation Division which amount to about 38% of the current funding to the Aviation Division. One of the distributions to the Aviation Division to be eliminated is the 4.79% of the taxable gross receipts attributable to the sale of jet fuel, while the other one is the 0.046% of Gross Receipts Tax distribution, which under current law sunsets in FY 2022.

The Human Services Department (HSD) provided the following analysis.

> There are two changes in the bill that have the potential of impacting the budget for the Medicaid program.
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> The funding for the County Supported Medicaid Fund and the Safety Net Care Pool will be funded by Gross Receipts taxes. While the funds are still appropriated to the Department for the Medicaid Program it is not clear if the amount identified in the bill will be equal to or greater that the current levels. In the FY20 Budget the County Supported Medicaid fund is anticipated to provide $32.5 million to match federal Medicaid funds and the Safety Net Care Pool is anticipated to provide $28.5 million for the same purpose. It is not clear if the fourteen thousandths percent for Medicaid Fund and the eighteen thousandths percent for the Safety Net Care Pool of the net receipts of gross receipts tax will be equal to or greater to the $61 million from those two sources. For every dollar of match from these two sources the Medicaid program can earn $3.55 dollars in Federal Medicaid Match.

The Higher Education Department (HED) provided the following analysis.

> Section 1. Amending Section 3-31-1 NMSA 1978 Revenue Bonds: Many of the higher education institutions throughout the state rely heavily on General Obligation Bonds and Severance Tax Bonds to fund their infrastructure maintenance. Building renewal and replacement funds are limited and removing the ability to impose or authorize a municipal higher education facilities gross receipts tax reduces the available funding mechanisms.
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> Section 7. Amending Section 4 – 48B-12 NMSA Tax Levies Authorized: Reductions to Mill Levy Revenues and Medicaid county transfers to the University of New Mexico Health Sciences Health Systems could negatively impact the operating budgets of these entities and thus reduce that ability to provide optimum levels of health care to citizens of New Mexico.
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> Section 81. Amending Section 27-5-6 NMSA 1978 Powers and Duties of counties relating to indigent care. The removal of item D and F which stipulate the amount of one fourth of the county's payment and the Medicaid transfers on specific dates could cause an adverse effect on timely and predictable deposits in to the Safety Net Care Pool Fund and the county supported Medicaid fund as required by the existing statewide Health Care Act. The statewide Health Care Acts serves to recognize that the counties of the

state are also responsible for supporting indigent patients by providing local revenues to match federal funds for the state Medicaid program, including the provision of matching funds for payments to sole community provider hospitals and the transfer of funds to the county-supported Medicaid fund pursuant to the Statewide Health Care Act. [27-10-1 to 27-10-4 NMSA 1978]

SIGNIFICANT ISSUES

The New Mexico Municipal League provided the following analysis.

Under this bill, all wage-earners become subject to the gross receipts tax. No explicit sourcing provision (place of work or residence) is made, letting TRD decide by rule. Since this seems a fundamental aspect of the entire scheme, it should not be left to agency discretion, especially without guidance.

The bill goes too far in cleaning out gross receipts tax credits at 7-9-79 and 7-9-79.1, which could very unnecessarily raise the specter of violation of interstate commerce rules.

The bill consolidates the several municipal and county gross receipts taxes by repealing what are today the main authorizing statutes and re-enacting them. Without a temporary (or other) provision specifying that the existing local option taxes continue in force, continuing to levy these taxes (including those that have been bonded) may become questionable.

NMDOT provided the following analysis.

The portion of the LVGRT distributed to the Highway Infrastructure Fund is a pledged revenue source for all DOT bond issues. Repealing the LVGRT will directly impact DOT's outstanding bonds. The Highway Infrastructure Fund is a restricted fund established in Section 67-3-59.2 NMSA 1978. If the LVGRT is repealed it will result in an impairment to all current outstanding bonds and will directly impact bond ratings and coverage ratios.

HED provided the following analysis.

Significant issues related to higher education:

1) Section 1. Amending Section 3-31-1 NMSA 1978 Revenue Bonds. SB358 would eliminate in its entirety paragraph J. Section 3-31-1 NMSA et. seq. governs the authority of municipalities to issue revenue bonds. Section 3-31-1 (J) allows municipalities to issue gross receipts tax (GRT) revenue bonds "for the purpose of acquisition, construction, renovation or improvement of facilities of a four-year post-secondary public educational institution located in the municipality and acquisition of or improvements to land for those facilities."

While this presumably would prevent municipalities from issuing gross receipts tax revenue bonds for the purpose of capital projects related to four-year postsecondary institutions, SB358 also modifies section 3-31-1 (D) to allow municipalities to issue GRT revenue bonds "for any municipal purpose". Moreover, 3-18-4 NMSA gives municipalities authority to construct, maintain and manage public buildings.

Pursuant to 12-1-21 NMSA; 21-13-14D NMSA; 21-14-12D NMSA; and 5.3.10 NMAC, the Higher Education Department reviews and approves all capital projects for higher education institutions prior to project initiation, irrespective of their funding source. HED is unaware of any municipally-issued GRT revenue bonds that support capital projects at public postsecondary institutions.

2) Section 7. Amending Section 4 – 48B-12 NMSA Tax Levies Authorized. SB358 amends existing language pertaining to the imposition and collection of mil levies to pay for the costs of operating and maintaining county hospitals or contracting hospitals in accordance with a health care facilities contract. It also strikes language specific to class "A" counties which pay for the county's transfer to the county supported Medicaid fund. If SB358 were to be enacted, paragraph D of this section would be eliminated, thus no longer requiring any class "A" county imposing the mil levy of this section to enter into a mutual agreement with a state educational institution operating the hospital, permitting the transfer to the county-supported Medicaid fund by the county. Instead it would add new language outlining the distribution of the mill levy authorized at the rates specified in Subsection A specified in parts 1 and 2, which shall be made to county and contracting hospitals as authorized in the "Hospital Funding Act." Additionally, language in parts 1 and 2 of subsection A eliminate language that meet the requirements of Section 27-10-4 NMSA 1978 – Public Assistance, alternative revenue source to imposition of county health care gross receipts tax; transfer to county-supported Medicaid fund or Section 7-37-7.1 NMSA 1978 – Additional limitations on property tax rates.

3) Section 45. Section 7-2C-3 NMSA1978 Tax Refund Intercept Program Act. SB358 includes language pertaining to claimant agency, which the New Mexico Higher Education Department is included. There are no changes to the stipulations that would affect NMHED. The amendment does however change the name of the Act which governs refunds, tax rebates or credits, from the Income Tax Act or the Corporate Income and Franchise to the Gross Receipts and Compensating Tax Act. Lastly the refund would be due to a tax payer, striking "an individual or corporation".

4) Section 49. Section 7-2C-11 NMSA 1978 (being Laws 1985, Chapter 106, Section 11, as amended) Priority of Claims also applies to NMHED, although there are no changes to the stipulation, it merely updates the name of the Act which governs refunds, tax rebates or credits, from the Income Tax Act or the Corporate Income and Franchise to the Gross Receipts and Compensating Tax Act.

5) Section 81. Amending Section 27-5-6 NMSA 1978 Powers and Duties of counties relating to Indigent Care. SB358 deletes paragraph D, which designates the transfer dates for the county's payments, equal to one fourth of the county's payment to be deposited in to the Safety Net Care Pool Fund. Additionally, paragraph F is deleted, which sets forth the transfer of money from the fund to the county supported medic-aid fund to meet the requirements of the Statewide Health Care Act.

ADMINISTRATIVE IMPLICATIONS

This bill would be challenging to implement, and TRD and other entities would face significant challenges to accommodate the quick effective date. It would likely cost many millions of dollars and possibly tens of millions of dollars to reprogram TRD software, update systems and forms, etc.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

This bill conflicts with nearly all other tax bills.

TECHNICAL ISSUES

In addition to technical issues with how the rate resetting is structured, there may be other technical issues. The New Mexico Municipal League reported the bill fails to reconcile 7-9-7A with 7-9-43F and should strike 7-9-7A(3).

Does the bill meet the Legislative Finance Committee tax policy principles?

1. **Adequacy**: Revenue should be adequate to fund needed government services.
2. **Efficiency**: Tax base should be as broad as possible and avoid excess reliance on one tax.
3. **Equity**: Different taxpayers should be treated fairly.
4. **Simplicity**: Collection should be simple and easily understood.
5. **Accountability**: Preferences should be easy to monitor and evaluate

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