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## FISCAL IMPACT REPORT

ORIGINAL DATE 1/27/2020

SPONSOR Papen LAST UPDATED \_\_\_\_\_ HB \_\_\_\_\_

SHORT TITLE Tax Deduction For Durable Med Equipment SB 39

ANALYST Graeser

### REVENUE (dollars in thousands)

| Estimated Revenue |           |           |           |           | Recurring or<br>Nonrecurring | Fund<br>Affected  |
|-------------------|-----------|-----------|-----------|-----------|------------------------------|-------------------|
| FY20              | FY21      | FY22      | FY23      | FY24      |                              |                   |
|                   | (\$730.0) | (\$750.0) | (\$770.0) | (\$800.0) | Recurring                    | General Fund      |
|                   | (\$490.0) | (\$500.0) | (\$515.0) | (\$530.0) | Recurring                    | Local Governments |

Parenthesis ( ) indicate revenue decreases

### ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

| FY20 | FY21 | FY22 | 3 Year<br>Total Cost | Recurring or<br>Nonrecurring | Fund<br>Affected |
|------|------|------|----------------------|------------------------------|------------------|
|      | 0    | 0    | 0                    | Recurring                    | TRD Operating    |

Parenthesis ( ) indicate expenditure decreases

### SOURCES OF INFORMATION

LFC Files

#### Responses Received From

Taxation and Revenue Department (TRD)

### SUMMARY

#### Synopsis of Bill

Senate Bill 39 extends the existing gross receipts tax deduction from the sale or rental of durable medical equipment and medical supplies until July 1, 2030. The deduction was set to expire on July 1, 2020. The bill changes the annual report requirement by the Taxation and Revenue Department (TRD) on the effectiveness and cost of the deduction to the Revenue Stabilization and Tax Policy Committee and the Legislative Finance Committee from being presented every five years to every year.

The effective date of this bill is July 1, 2020. There is no explicit delayed repeal date but there is an implicit sunset (terminal effective date for transactions) of July 1, 2030.

**FISCAL IMPLICATIONS**

This bill may be counter to the LFC tax policy principle of adequacy, efficiency, and equity. Due to the increasing cost of tax expenditures, revenues may be insufficient to cover growing recurring appropriations.

Generally, estimating the cost of tax expenditures is difficult. However, this durable medical equipment GRT deduction was one of the earliest to require specific reporting of the deduction by statutory citation.

TRD notes the methodology for the estimate: “The durable medical exemption is separately reported in GenTax (the TRD system of record), actuals from Fiscal Year 2019 were used in the calculation and grown by inflation figures provided by Global Insight, a national economic forecasting group.”

LFC staff, however, note that the original FIR in 2014 (HB56/aHTRC) used a survey method of estimating the impact. The revenue table at that time follows:

| Estimated Revenue |                    |                    |                    |                    | Recurring<br>or<br>Nonrecurring | Fund<br>Affected  |
|-------------------|--------------------|--------------------|--------------------|--------------------|---------------------------------|-------------------|
| FY14              | FY15               | FY16               | FY17               | FY18               |                                 |                   |
| \$0.0             | (\$1,735.0)        | \$(1,774.0)        | (\$1,815.0)        | (\$1,854.0)        | Recurring                       | General Fund      |
| \$0.0             | (\$1,157.0)        | (\$1,183.0)        | (\$1,210.0)        | (\$1,236.0)        | Recurring                       | Local Governments |
| <b>\$0.0</b>      | <b>(\$2,892.0)</b> | <b>(\$2,957.0)</b> | <b>(\$3,024.0)</b> | <b>(\$3,089.0)</b> |                                 | <b>Total</b>      |

From the FIR of the 2014 bill:

With the assistance of industry groups, TRD identified 54 New Mexico durable medical equipment suppliers licensed by Medicare and Medicaid whose sales are no less than 90 percent prescribed durable medical equipment (DME) or prescribed medical supplies. About 40 of those filed gross receipts tax returns in FY13. Based on TRD data, these 40 entities reported approximately \$39.3 million dollars in taxable gross receipts and \$2.8 million in gross receipts tax in FY13.

Note that the FY18-FY19 actual data as reported was about half the amount initially estimated. This could be a report card on the accuracy of the voluntary reporting of specific statutory citation on the CRS-1 report. This discrepancy may indicate the difficulty that TRD will have implementing further specific reporting requirements.

**SIGNIFICANT ISSUES**

This bill narrows the gross receipts tax (GRT) base. Many of the efforts over the last few years to reform New Mexico’s taxes focused on broadening the GRT base and lowering the rates. Narrowing the base leads to continually rising GRT rates, increasing volatility in the state’s largest general fund revenue source. Higher rates compound tax pyramiding issues and force

consumers and businesses to pay higher taxes on all other purchases without an exemption, deduction, or credit.

TRD makes similar comments:

This bill would extend a currently existing deduction that reduces the expenses for durable medical equipment and oxygen supplies. The current deduction and proposed extension limit overall cost by reducing equity across business types, the deduction is limited to companies with 90 percent of their sales from durable medical equipment, excluding sales from grocery stores, large retailers, and most pharmacies. From a public good standpoint, it reduces the cost of this equipment for consumers. Tax expenditures narrow the tax base, and may require increases in taxes in other areas, a reduction in government services, or both.

## PERFORMANCE IMPLICATIONS

The LFC tax policy of accountability is met with the bill's requirement to report annually to an interim legislative committee regarding the data compiled from the reports from taxpayers taking the deduction and other information to determine whether the deduction is meeting its purpose. However, refer to the discussion at FISCAL IMPLICATIONS that the annual report to the legislature may not be as accurate as desired.

## CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

Duplicates HB109.

## OTHER SUBSTANTIVE ISSUES

The increasing prevalence of Internet and interstate sales of durable medical equipment may mean that domestic purveyors of this equipment are at a considerable commercial disadvantage – particularly if the in-state sellers must pay the GRT because they do not qualify for the deduction. In some ways, this deduction is not only a means of reducing the overall cost of medical care, but may also serve to assist economic development in a rapidly growing sector of the economy.

### **Does the bill meet the Legislative Finance Committee tax expenditure policy principles?**

- 1. Vetted:** The proposed new or expanded tax expenditure was vetted through interim legislative committees, such as LFC and the Revenue Stabilization and Tax Policy Committee, to review fiscal, legal, and general policy parameters.
- 2. Targeted:** The tax expenditure has a clearly stated purpose, long-term goals, and measurable annual targets designed to mark progress toward the goals.
- 3. Transparent:** The tax expenditure requires at least annual reporting by the recipients, the Taxation and Revenue Department, and other relevant agencies.
- 4. Accountable:** The required reporting allows for analysis by members of the public to determine progress toward annual targets and determination of effectiveness and efficiency. The tax expenditure is set to expire unless legislative action is taken to review the tax expenditure and extend the expiration date.
- 5. Effective:** The tax expenditure fulfills the stated purpose. If the tax expenditure is designed to alter behavior – for example, economic development incentives intended to increase economic growth – there are indicators the recipients would not have performed the desired actions “but for” the existence of the tax expenditure.

**6. Efficient:** The tax expenditure is the most cost-effective way to achieve the desired results.

**WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL?**

| <b>LFC Tax Expenditure Policy Principle</b> | <b>Met?</b> | <b>Comments</b>   |
|---|-------------|---|
| <b>Vetted</b>                               | ✓           | Extension of a 2014 deduction.  |
| <b>Targeted</b>                             |             |   |
| Clearly stated purpose                      | ?           | No purpose stated; reduce medical costs purpose inferred.   |
| Long-term goals                             | ✗           | None stated.  |
| Measurable targets                          | ✗           | None stated   |
| <b>Transparent</b>                          | ?           | TRD has not reported the expenditures in the Tax Expenditure Report, but has provided the expenditure numbers for this FIR. |
| <b>Accountable</b>                          |             |   |
| Public analysis                             | ?           | The initial 2014 bill analysis was performed cooperatively with industry.   |
| Expiration date                             | ✓           | Implicit for sales after July 1, 2030   |
| <b>Effective</b>                            |             |   |
| Fulfills stated purpose                     | ✗           | No purpose stated   |
| Passes “but for” test                       | ?           | Probably not applicable.  |
| <b>Efficient</b>                            | ?           | May be the only tool available to state policy makers to reduce medical costs.  |
| Key:    ✓ Met    ✗ Not Met    ? Unclear     |             |   |

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