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FISCAL IMPACT REPORT

		ORIGINAL DATE	1/30/22		
SPONSOR	HCEDC	**LAST UPDATED**	2/9/22	**HB**	129/HCEDCS
SHORT TITLE	Business Income By Single Sales Factor			**SB**	
				ANALYST	Graeser

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY22	FY23	FY24	FY25	FY26		
*Indeterminate but Negative						General Fund-(PIT)
*Indeterminate but Negative						General Fund- (CIT)

Parenthesis ( ) indicate revenue decreases
*The fiscal implications of this bill are very complicated and will require substantial additional study. See FISCAL IMPLICATIONS for a preliminary assessment of these impacts.

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

FY22	FY23	FY24	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
	$7.7		$7.7	Nonrecurring	ITD – Staff workload costs

Parenthesis ( ) indicate expenditure decreases

SOURCES OF INFORMATION
LFC Files

Responses Received From
Economic Development Department (EDD)
Taxation and Revenue Department (TRD)

SUMMARY

Synopsis of Bill

House Commerce and Economic Development Committee Substitute for House Bill 129 repeals the use of the three-factor formula apportionment of multi-state income in favor of a single sales factor formula apportionment for most corporations and pass-through entities. This puts most C-corporations on equal footing, not just manufacturing corporations or corporations with headquarters in New Mexico.

However, this proposal would have uneven effect between primarily New Mexico corporations and national/multinational corporations with limited sales in New Mexico and would not impose any additional liability on non-nexus corporations with any level of sales in New Mexico.

The substitute bill allows eligible corporations or pass-through entities to elect to retain the traditional three-factor formula or adopt the single sales factor apportionment if that reduces corporate or personal income tax liability. Once the election is made, it is permanent. Corporations may not switch between these two methods. A qualifying entity for the purpose of the election is one with the following characteristics:

1. It is a business unit of a corporation or a group of corporations in a combined filing group;
2. This business unit must have 100 or more payroll employees in New Mexico on the first day of the taxable year one year prior to the election year (for most calendar year corporations, this would be the number of employees on January 1, 2022); and
3. With a cumulative investment in New Mexico exceeding $50 million as measured by the original basis for tax purposes plus any subsequent investment minus any dispositions.

Currently, with a few exceptions for corporate headquarters or manufacturing, corporations and pass-through entities (PTEs) apportion their U.S. income to New Mexico using the average of a property, payroll, and sales factors. Essentially, each of these factors is the percentage of New Mexico property, payroll, or sales to the corresponding U.S. total property, payroll, or sales. This bill proposes to abandon this venerable three-factor apportionment formula and only consider sales ratios. This will, in general, provide additional liability for national and international corporations with moderate physical presence, but will provide very substantial tax deductions for businesses that have relatively large ratios of property and payroll ratio relative to the sales ratio. This provision is intended to incentivize national and international corporations to build plants and facilities in New Mexico and hire New Mexico workers, but export the New Mexico produced products or services out of the state. However, the bulk of the tax reductions will affect the OGAS sector that has very large property and payroll factors, but very low sales factor.

The effective date of this bill is January 1, 2024. The provisions of the bill are applicable to tax years beginning January 1, 2023, with fiscal effects realized primarily in FY25, since most C corporations do not file until October of the year following the tax year. The bulk of the impact from PTEs will also be realized in FY25, but some fraction will be realized in FY24.

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.

Estimating the cost of tax expenditures is difficult, both for FIR purposes and in determining the cost of tax expenditures after enactment and implementation. Confidentiality requirements surrounding certain taxpayer information create uncertainty, and analysts must frequently interpret third-party data sources. The statutory criteria for a tax expenditure may be ambiguous, further complicating the initial cost estimate of the expenditure's fiscal impact. Once a tax expenditure has been approved, information constraints continue to create challenges in tracking the real costs (and benefits) of tax expenditures.

This bill could have negative general fund impact approaching ($20,000.0) pursuant to the following reasoning:

1. Section 1 of the bill amends Section 7-4-10 NMSA 1978, "Apportionment of Business Income".

2. Section 7-4-10 NMSA 1978 currently provides rules, with several exceptions, for apportioning ***all business income*** to this state by multiplying the income by a fraction, the numerator of which is the property factor plus the payroll factor plus the sales factor and the denominator of which is three. Note that Section 7-4-10 NMSA 1978 does not reference organizational structure in the apportionment rule. If multistate business is conducted by C corporations, Sub S corporations, LLCs, LLPs, MLPs or other pass-through entities (PTEs) the provision of this bill would apply.
3. It is expected that replacing the three factor apportionment with single sales might be a boon for OGAS producers. Large producers with investments in many states would probably see a reduction in taxes because the sales factor would be close to zero (unless the “throwback rule” of 7-4-17 NMSA 1978 applied, since the sales point for crude oil is at Cushing, Oklahoma. Texas does not have an income tax, so a sale at Cushing might be thrown back to Oklahoma or New Mexico) and both property and payroll factors would be significant – up to 100%. The situation for PTEs is less certain. Many LLCs or LLPs own a share of a number of wells, but those wells tend to be all within the state. The apportionment change from the three-factor formula to single sales would not affect these PTEs. 100% of the payment would be apportioned to New Mexico. The “throwback rule” of 7-4-17 NMSA is a highly technical point and cannot be accurately determined.
4. OGAS withholding taxes are imposed (7-3A NMSA 1978) on certain payments by in-state remitters to out-of-state residents, whether as individuals or members of various PTEs. The level of these OGAS Withholding taxes are currently in the range of $180 million. Because this withholding is imposed on out-of-state residents with in-state business income, this total may be a good base for determining the current level of income taxes and the impact of replacing the three-factor apportionment with a single sales factor. However, there are many PTEs that only own a share of wells, all of which are in New Mexico. The provisions of this bill only affect businesses with income in New Mexico and at least one other state. While TRD can identify multi-state OGAS producers for corporate income tax, this determination for PTEs is very difficult and cannot be done by querying the returns database.
5. Businesses with 100 percent of property, payroll, and sales would have no change in PIT or CIT liability. Note: PTEs report on personal income tax returns (PIT) and C corps report on corporate income tax returns.
6. Without a change in the corporate income tax nexus rules, such as changing to an economic nexus, corporations without significant physical presence in the state would continue to avoid any corporate income tax liability even with the changes in apportionment formula of this bill. (See further discussion of the uncertainties posed by corporate income tax nexus at OTHER SUBSTANTIVE ISSUES).
7. The bill would replace the three-factor formula with a single sales factor. This is the ratio of sales in New Mexico divided by total sales in all states (water’s edge election). Industries with payroll or property factors greater than sales factor would have tax reductions. See table below for examples of various businesses affected positively or negatively by the change in apportionment.
8. The amendment allows “eligible businesses” the option of retaining the three-factor formula or adopting a sales-only apportionment. The assumption here is that all businesses will adopt an apportionment formula that reduces or maintains taxes. This divides the universe further:

Class of Business	Direction of Change	Examples
Businesses with 100% of property, payroll and sales in state.	No change	Most small businesses; most franchise businesses, incl new car dealers; banks; incl many/most PTEs;
Currently tax favored businesses that can elect 3-factor or single sales	Liabilities will be the same as current law	Manufacturers and companies with a regional or national headquarters in the state
National/international corporations without physical presence	No current liability; no change in liability.	Out-of-state manufacturers; franchise parent companies; remote sellers/internet sellers/catalog companies.
Eligible businesses electing single sales or 3-factor formula	Liabilities will decrease or stay the same	Most national retail chains; larger motels/hotels, electric utilities; telecoms/internet utilities; national laboratories; any business employing > 100 payroll employees (assume $50 million investment). May include large OGAS producers.
Non-eligible businesses with property and payroll factors less than sales factor	Liabilities will increase	Most national/international businesses with economic nexus, but little on-site presence; HBO subscription;
Non-eligible businesses with property and payroll factors greater than sales factor	Liabilities will decrease	Most OGAS businesses; film production companies; renewable energy production.

A general conclusion is that with the election, all eligible/qualifying business entities that sell product or services in New Mexico and in other states will have reduced or identical tax liability, depending on whether the election changes each entity's apportionment formula and irrespective of business organizational structure. This acknowledges that the impact may be negative because corporations and PTEs doing business in at least two states will choose the apportionment method that reduces tax liability. This bill only applies to apportionment of multi-state income, so for New Mexico corporations and PTEs that have all their sales, property, and payroll in this one state, there will be no change from current law.

The primary impact of this bill will be for regular C corporations. The 100 person payroll employment and $50 million investment in the state may effectively exclude most PTEs from the election. Five of the six categories in the table above can be estimated with the certainty that liabilities pursuant to the provisions of this bill will be reduced or stay the same. There is enormous uncertainty, however, for non-eligible businesses with property and payroll factors less than sales factors. This may apply to the bulk of consumption of goods and services. See OTHER SUBSTANTIVE ISSUES for a discussion of corporate income tax nexus and the movement in other states to measure corporate income tax nexus on an economic basis, rather than physical presence. The following assumes that the bulk of C corporations with no physical presence would not be liable for New Mexico corporate income taxes.

	FY 22	FY23	FY24	FY25	FY26
Gross CIT	$187.6	$168.7	$203.8	$209.1	$216.3
OGAS portion*		$25.3	$30.6	$31.4	$32.4
OGAS/PTE withholding	$195.7	$208.8	$183.8	$180.1	$180.8
Estimated non-eligible, multistate OGAS/PTE portion	$195.7	$20.88	$18.38	$18.01	$18.08
Negative impact from OGAS C Corps (Thousands)**			($26,000.0)	($30,700.0)	($31,500.0)
Negative impact from other eligible C Corps (Thousands)			Overall, may conform to TRD's point about the state being a market state.		
Positive impact from non-eligible C Corporations (Thousands) with nexus and sales factor > property and payroll factors			$20,000.0	$25,000.0	$25,000.0
Negative Impact from OGAS PTEs (Thousands)			($15,600.0)	($18,300.0)	($18,000.0)

Negative Impact from eligible PTEs (Thousands)	($1,000.0)	($1,000.0)	($1,000.0)
Positive impact non-eligible PTEs (Thousands)	$2,000.0	$2,000.0	$2,000.0
Net estimated maximum fiscal impact (CIT)	($6,000.0)	($5,700.0)	($6,500.0)
Net estimated maximum fiscal impact (PIT) from PTEs	($20,600.0)	($23,000.0)	($23,500.0)

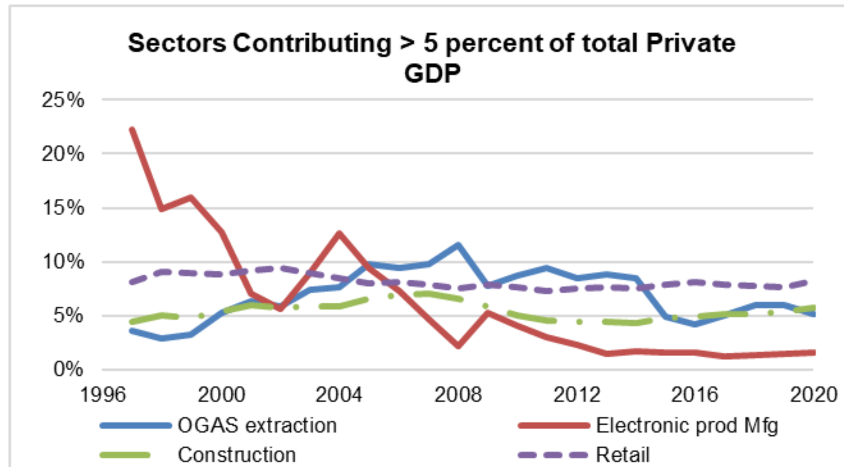
The January 2022 Consensus Revenue Estimate for gross corporate income tax and CIT refundable credits (primarily film production tax credit) is shown.

Revenue Source ($ Millions)	FY22	FY23	FY24	FY25	FY26
Gross Corporate Income Tax	**187.6**	**168.7**	**203.8**	**209.1**	**216.3**
CIT Refundable Credits	**(102.6)**	**(133.7)**	**(160.2)**	**(160.2)**	**(160.2)**
NET Corporate Income Tax	**85.0**	**35.0**	**43.6**	**48.9**	**56.1**

Note that the history of the gross corporate income tax is closely correlated to the profitability of four sectors: the oil and gas production sector, the computer and electronic products sector, construction, and big-box retail.[1]

- While some of firms sell product in the state, the vast majority of sales of crude oil occur at Cushing Oklahoma and sales of natural gas are in Louisiana at Henry Hub. To whatever extent this correlation implies actual profits in the industry, the bulk of the profits would escape taxation pursuant to the provisions of this bill. This industry may realize significant benefit from the provisions of this bill. This is true irrespective of the form of business.
- The computer and electronic products sector has been in secular decline over the years, judging from the contribution of this industry to state gross domestic product (GDP). Most of the production of this sector is exported, so the sales factor is close to zero. However, the provisions of this bill will not give any additional benefit to this sector, since manufacturing for export already enjoys the benefits of single factor sales apportionment.
- The construction industry is dominated by New Mexico firms. All three factors (Property, Payroll and Sales) under current law are close to 100 percent. Choosing the single sales factor would not change the CIT liability in this sector significantly.
- Retail is now dominated by national corporations: all big box retail, most food stores, building supplies, office supplies and department stores. All of these entities have physical presence and current liability depending on total corporate profitability. The accommodations industry is dominated by national/international corporations, although many nationally branded restaurants are in-state franchises quite separate from the CIT liability of the franchisor entity. Most of these retail businesses would become eligible for the election. Taking these factors together, it is difficult to determine if the sector would experience a decrease or no change in corporate taxes from the provisions of this bill. The key is whether the sales factor is substantially different from the payroll factor or the property factor.

[1] It might be interesting to solicit testimony from some of the new entrants to New Mexico to determine if these new national/international corporations would find the provisions of this bill beneficial.



A substantial number of business entities in New Mexico conduct business as a pass-through entity, not a Subchapter C (regular) corporation. Alternative organizational structures include sole proprietorships, partnerships, limited liability company (LLC), limited liability partnerships (LLP), master limited partnerships (MLP) and Subchapter S corporations (Sub S corps). These alternative structures are generally pass-through entities (PTEs) that have only one level of taxes – generally reported eventually on the owners' personal income tax returns.[2] If these businesses sell product or services in New Mexico and other states or countries, the provisions of this bill would apply. There will be some professional corporations that would qualify as eligible with over 100 payroll employees and $50 million in investment in the state for the permissive election.

However, the HCEDC substitute bill provides an election for eligible corporations and PTEs operating in at least two states to retain the three-factor apportionment or adopt single sales if that is more advantageous. Because of the election and the fact that PTEs may be conducting business in more than one state, the overall impact of the substitute bill must generally be negative for eligible businesses and positive for non-eligible businesses and neutral for businesses with 100 percent of sales, property and payroll in New Mexico.

SIGNIFICANT ISSUES

There are three arguments advanced in favor of this proposal

1. Because Texas has no corporate income tax, New Mexico is relatively unattractive on this criterion for national or international corporations to establish a presence in the state in comparison to similar location or expansion in Texas. This may be an impediment to economic development. If so, business taxes add to the low personal income of state residents and low population density of the state. With the provisions of this bill, New Mexico will increase its attractiveness for manufacturers and other corporations that have significant property and payroll in the state, but sell a substantial portion of their product or service outside the state. Since manufacturers can elect the single sales factor under current law, this argument in favor may be limited. However, this change will improve the image of New Mexico as being "open for business";

[2] A single member limited liability company (LLC) may file as a sole proprietorship (PTE) or as a Sub C or Sub S corporation. A multi-member LLC may file as a partnership (PTE) or as a Sub C or Sub S corporation.

2. This moves New Mexico toward a more current mainstream corporate tax. The dual tax imposed on corporate profits is seen by many observers as unfair and overly opportunistic. Allowing an election while retaining the mainstream single sales apportionment for most corporations may be the best of all worlds. Corporations and PTEs that are creating value in New Mexico are advantaged and other corporations that are not creating value in New Mexico are not damaged compared to how they would be treated in other states that impose corporate and PTE taxes; and
3. With the election for eligible entities, corporations and PTEs that are creating value in New Mexico will be given a significant tax break.

There are, similarly, three principal issues advanced in opposition to this proposal:

1. Compared to the original bill's provisions, this would not simplify an overly complex corporate income tax or the PTE reporting provisions of PIT. Some multi-national firms and most New Mexico firms complain about the very complex (and possibly unfair) gross receipts tax more than they complain about the corporate income tax or the taxes on pass-through entities.
2. New Mexico small businesses will experience no benefits from the provisions of this bill if all property, payroll and sales are in New Mexico.
3. The overall general fund cost of the proposal without any expectation of improvements in the state's economy may render the risk untenable.

EDD notes that the impacts of the provisions of this bill may be uneven, but generally supportive of economic development:

> "Single sales factor apportionment is a growing trend in state-level corporate income taxation, particularly in the western United States. This would create an even playing field with many other states. It would benefit corporations with most or all their income located outside of New Mexico, and it would not penalize any larger corporations with significant sales inside the state because of the provision allowing these larger corporations to continue using multi-factor apportionment."
>
> "This results in a generally friendlier business climate in the state for economic base companies and allows New Mexico to be competitive with surrounding states in attracting new businesses."
>
> "However, this bill would penalize any smaller corporations in New Mexico with multi-state income but with a high percentage of sales in this state. It is impossible to estimate how many businesses in New Mexico would be impacted, but they would have to file corporate income taxes (as opposed to other business formations that would provide for filing under personal income tax), have fewer than 100 employees, and have a relatively high percentage of multi-state sales occurring in New Mexico."

TRD, expanded on these speculations and considerations:

> "Corporations and the economy like certainty and that applies to the tax code. Changing the tax code and in this case the apportionment code for what would be the eighth time since it was enacted in 1983 reflects a level uncertainty as to the stability of the tax code. This uncertainty is seen by corporations as creating a less favorable business environment; on the other hand, most corporations do prefer to use the single sales factor test."

"On the other hand, having a single-sales factor reduces the complexity of the CIT code. This change would support the tax policy principle of simplicity were it not for the fact that some corporations can elect to remain at the three-factor election. Taxpayers incur compliance burdens as they prepare, submit, and keep records about tax returns. Likewise, Tax & Rev incurs administrative costs to collect taxes, review the accuracy of tax returns and tax payments, and bring taxpayers into compliance. The reduction of apportionment from three factors to one simplifies the tax code for both taxpayers and Tax & Rev. But by leaving the three-factor election, Tax & Rev continues to have a complex code to administer. The more complicated the code, the higher the cost everyone must bear to ensure compliance."

"The option of remaining at a three-factor formula for qualifying entities does not support the tax policy principle of equity. In 2013, legislation added the single-sales factor apportionment election for manufacturers, followed in 2015 by the single-sales factor apportionment election for companies with their headquarters in New Mexico. Were all corporations able to use a single-sale factor, all corporations would be treated equally in the tax code. This bill allows a carve-out from the single-sales factor formula thereby treating these taxpayers differently."

"A single sales factor for all corporations would arguably make New Mexico a more competitive environment compared to other states with a similar application of a single sales factor or no corporate income tax at all, although the data regarding the effect of moving to a single sales factor on competitiveness is inconclusive. Most states have moved to a single sales factor for purposes of income apportionment. As of January 2022, of states with CIT, only four states including New Mexico used the traditional three-factor formula, while 30 states and the District of Columbia used only sales in their apportionment formula[3]. The remaining states with a corporate income tax used a formula that gave greater weight to sales. "By using the portion of a corporation's sales rather than employment or property to determine tax liability, states hope to encourage companies to relocate or to expand their production operations within the states they operate in."[4] By shifting the burden of taxation to out-of-state companies, the single sale factor apportionment method theoretically encourages companies to set up their physical plant and locate employees in states that do not apportion based on these two factors. Again, however, the data are inconclusive as to whether states moving to a single sales factor apportionment have actually seen increased economic growth and investment. In a competitive environment, New Mexico's continuing use of the three-factor apportionment test may place it at a disadvantage for companies to form or relocate here. (However, it is also true that corporations look to more than just the tax code when considering operations. These include among other things, the work force skill-level and education, infrastructure, and education systems.)"

"The three-factor apportionment test is also not well adapted to the contemporary economy. Historically, the three factors were meant to represent the profits attributable to labor (employment), capital (physical plant), and market (sales). In an economy that is

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[3] Federation of Tax Administrators, January 2022

[4] https://www.urban.org/policy-centers/cross-center-initiatives/state-and-local-finance-initiative/projects/state-and-local-backgrounders/corporate-income-taxes

increasingly service-oriented and based on the internet, investment in physical plant no longer has the importance in generating profit for companies that it once did. Profits are less attributable to the location of physical plant in one state, and therefore assume less importance in deciding how to apportion income to each state. Increases in productivity also mean that businesses can do more with a smaller payroll, decreasing the importance of the payroll factor."

"But, this bill allows for some corporations to remain under the three-factor apportionment while other corporations overall transition to a single-factor, continuing to place New Mexico in the minority of states who continue to maintain the three-factor appointment as a possible election."

PERFORMANCE IMPLICATIONS

The LFC tax policy of accountability is not met since TRD is not required in the bill to report annually to an interim legislative committee regarding the data compiled from the reports from taxpayers taking advantage of the provision to determine whether the single sales factor is meeting its economic development purpose, simplification purpose or revenue generating purpose.

ADMINISTRATIVE IMPLICATIONS

"The proposal will have a low impact on TRD's Information Technology Division (ITD) of approximately 150 hours or about 1 month of development work at approximately $7,746. TRD will update forms, instructions, and associated publications. These updates will be incorporated into annual tax program revisions. TRD will also need to update NMAC regulations to match the statutory changes.

TECHICAL ISSUES

Generally, for the possible changes of this magnitude in any revenue source, LFC recommends a delayed repeal to allow analysis of the long-term benefits of the provisions of this bill. However, mindful of the numerous changes in the corporate income tax since 1983, the provisions of this bill tend to stabilize the corporate income tax and position the tax to a more mainstream consensus as to the proper way of taxing corporate and business profits within an increasingly global milieu.

TRD has identified a number of technical issues:

On Page 5, line 24 and 25 "quantifying entity" is defined as having the presence of a "business unit of a corporation", business unit is not defined and leaves this portion of the law subject to interpretation. Without a definition this may cause inconsistent use of this method and may require further guidance by adding regulations after the fact. Tax & Rev suggests reference to the IRS code where "Qualified Business unit" is defined under 26 U.S.C.A. § 989(a.) – "For purposes of this subpart, the term "qualified business unit" means any separate and clearly identified unit of a trade or business of a taxpayer which maintains separate books and records."

On page 6, line 2 and 3, the bill states "with one hundred or more employees for whom wages are withheld." Tax & Rev suggests the rewriting of this reference to refer to

withholding of wages for income tax liability, for example, "with one hundred or more employees for whom income taxes are withheld against wages."

On page 6, line 6, the bill language states that the employment measurement date once election is selected is to be certified by audit. It is unclear what is meant by 'audit,' as in certified by the Audit and Compliance Division of Tax & Rev or an independent audit to obtain a certification. Tax & Rev recommends that the election or certification is done using a method prescribed by the department.

Tax & Rev notes that Section 7-4-17(B)(2) NMSA 1978 needs to be amended because it refers to existing 7-4-10 (B) and (C). In addition, Section 7-4-19 NMSA 1978 will require amending as it refers to if the apportionment does not represent the extent of the taxpayer's activity in New Mexico, one or more factors may be eliminated.

OTHER SUBSTANTIVE ISSUES

Understanding the fiscal impact of this bill requires simultaneous understanding of a number of tax concepts and sections of statute. At minimum, this involves an analysis of Section 7-3A Oil and Gas Proceeds and Pass-Through Entity Withholding Tax and the "throwback rule" of Section 7-4-17 (Determination of sales in this state of tangible personal property for inclusion in sales factor); and the concept of "nexus" for imposition of income taxes.

Pursuant to Section 7-3A, "oil and gas proceeds" means any amount derived from oil and gas production from any well located in New Mexico and payable as royalty interest, overriding royalty interest, production payment interest, working interest or any other obligation expressed as a right to a specified interest in the cash proceeds received from the sale of oil and gas production or in the cash value of that production, subject to all taxes withheld therefrom pursuant to law. "oil and gas proceeds" excludes "net profits interest" …

Pursuant to Section 7-3A-3, remitters must withhold taxes from payments of oil and gas proceeds to the remittee. This withholding requirement is waived if the remittee is resident in New Mexico. Note, however, that only oil and gas proceeds are subject to this withholding and no other payments for business activities to out-of-state residents are subject to withholding.

Section 7-4-17 provides that sales of tangible personal property are in this state if the property is shipped from a place of storage in this state and the taxpayer is not taxable in the state of the purchaser. This is known as the "throwback rule" and might apply to sales of crude oil at Cushing, Oklahoma by a taxpayer resident in Texas. Texas has no income tax.

A particularly vexing understanding is for corporate income tax nexus[5]
To tax an out-of-state business a state must show that nexus exists between it and the business' income producing activities. Although many states are now adopting the factor presence standard to figure out if nexus exists, New Mexico retains the traditional physical presence standard.

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[5] https://www.wolterskluwer.com/en/expert-insights/income-tax-factor-presence-nexus-standard#:~:text=Nexus%2C%20a%20connection%20between%20a,state%20to%20impose%20income%20tax.&text=States%20using%20the%20economic%20presence,physical%20presence%20in%20the%20state.

Under factor-based nexus, or factor presence nexus, an out-of-state company has nexus if it has property, payroll, or sales that exceed certain thresholds during the tax period. The Multistate Tax Commission (MTC) adopted a factor presence nexus standard model statute. The model includes threshold amounts to use in determining if enough substantial nexus exists to subject a business to state income tax. Factor presence nexus provides an easily ascertainable standard.

Factor Presence Standard Thresholds
Under the MTC's factor presence nexus standard, a company is doing business in a state if the property, payroll, or sales exceed these thresholds during the tax period:

- $50,000 of property;
- $50,000 of payroll;
- $500,000 of sales; or
- 25% of total property, total payroll, or total sales.

Addition explanation:
Many states are moving to economic nexus for corporate income taxes. The fact that New Mexico has not moved in this direction renders a fiscal estimate of the provisions of this bill quite uncertain. Thompson Reuters[6] explains the issues as follows:
"Many states now require out-of-state companies to collect and remit sales taxes on in-state purchases, and more are invoking economic nexus standards in the corporate income tax area as well."

"In *South Dakota v. Wayfair, Inc.*, the U.S. Supreme Court ruled that states can levy taxes on sales even when the seller does not have a physical presence in the state. This overturned a previous ruling (*Quill v. North Dakota)* which required some form of in-state physical presence by an out-of-state company before that company could be subject to the sales- and use-tax nexus requirements of the state."

"Following *Wayfair*, most states passed legislation requiring out-of-state companies to collect and remit sales taxes on in-state purchases — and now several states are invoking economic nexus standards in the corporate income tax area as well. At least **six states** — Hawaii, Washington, Oregon, Massachusetts, Texas, and Pennsylvania — have amended their corporate income tax regulations to reflect the level of economic activity companies have in their jurisdictions. For the most part, the new rules will go into effect for the 2020 tax year, and more states and municipalities are likely to follow suit."

"Generally, state economic nexus statutes require a specific minimum amount of revenue linked to the particular state *before* nexus is established. For taxpayers, determining when a state's revenue threshold has been met can be challenging when it comes to sourcing revenues that arise from the sale of services. Sourcing of such sales is a critical element in the determination of where a company is liable for filing income tax returns because it has established economic nexus."

"And because an ever-increasing portion of our economy is generated through the provision of services, having a clear understanding of how services are sourced is mandatory in performing a nexus analysis."

[6] https://www.thomsonreuters.com/en-us/posts/tax-and-accounting/economic-nexus-corporate-income-taxation/

POSSIBLE QUESTIONS

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.

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.

LFC Tax Expenditure Policy Principle	Met?	Comments
Vetted	✘	This is the first time this particular proposal has been offered.
Targeted		
Clearly stated purpose	✘	The unstated purpose of this bill is economic development. However, no measureable targets have been offered toward unstated economic development goals.
Long-term goals	✘	
Measurable targets	✘	
Transparent	✘	It will be very difficult to measure progress toward improvements in the state's economy attributable to the provisions of this bill. There are many other factors – personal income, skilled workforce, educational attainment, clean air and water, quality of life, and so on that affect corporate expansion decisions.
Accountable		
Public analysis	✘	None.
Expiration date	?	Not provided and may not be appropriate.
Effective		
Fulfills stated purpose	✘	
Passes "but for" test	✘	
Efficient	?	This may be more efficient than "trying to pick winners using tax policy."

Key: ✓ Met ✘ Not Met ? Unclear

LG/al/acv/rl/al