BILL ANALYSIS AND FISCAL IMPACT REPORT
Taxation and Revenue Department

February 12, 2025

Bill: SB-141 **Sponsor:** Senators Peter Wirth and Roberto "Bobby" J. Gonzales, and Representative Cristina Parajon

Short Title: $100,000 Standard GRT Deduction

Description: This bill amends Section 7-2A-5 NMSA 1978 to increase the corporate income tax rate to 6.9% of taxable income. It also amends Section 7-9-3.3 NMSA 1978 to strike the word "taxable" when establishing the threshold for economic nexus to determine which taxpayers without physical presence in the state are engaging in business for the purpose of the gross receipts tax. The bill also adds a new section to the Gross Receipts and Compensating Tax Act providing a deduction from gross receipts for a taxpayer that did not claim any credit, deduction or exemption pursuant to the Gross Receipts and Compensating Tax Act (GRCTA) in the previous calendar year and was engaging in business in each month of the previous calendar year. The deduction is up to $100,000 of the taxpayer's receipts. The bill contains anti-abuse provisions to deter companies from splitting their operations or changing their corporate structure to claim additional deductions under this section (see Administrative Impacts). The bill also appropriates $100,000 from the general fund to the Taxation and Revenue Department (Tax & Rev) for expenditure in fiscal years 2025 and 2026 for administering the gross receipts tax deduction portion of the bill.

Effective Date: January 1, 2026. Applicable to taxable years beginning on or after January 1, 2026.

Taxation and Revenue Department Analyst: Lucinda Sydow and Pedro Clavijo

Appropriation*		R or NR**	Fund(s) Affected
FY2025	FY2026		
$100	$100	NR	General Fund - Tax & Rev

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

Estimated Revenue Impact*					R or NR**	Fund(s) Affected
FY2025	FY2026	FY2027	FY2028	FY2029		
--	--	$164,000	$168,200	$173,000	R	Section 1: General Fund
--	(Unknown but negative. See narrative)				R	Section 2: General Fund
--	(Unknown but negative. See narrative)				R	Section 2: Local Governments
--	($182,100)	($187,800)	($192,700)	($199,000)	R	Section 3: General Fund
--	($121,400)	($125,200)	($128,500)	($132,700)	R	Section 3: Local Governments
--	($182,100)	($23,800)	($24,500)	($26,000)	R	Total General Fund

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

Methodology for Estimated Revenue Impact:

[**Section 1:**] Tax & Rev calculated the estimated Corporate Income Tax (CIT) tax base based on the Consensus Revenue Estimating Group (CREG) December 2024 forecast. Tax & Rev then applied the

higher 6.9% tax rate on the base and calculated the net growth in revenue. This tax base includes the estimated revenue from pass-through entity (PTE) filers who as of FY24 are now included in the revenue under CIT. Per Section 7-3A-10(C) NMSA 1978, these taxpayers who have elected the entity-level tax will pay income tax liability at the higher of the maximum tax rate under Personal Income Tax (PIT), 7-2-7 NMSA 1978 or under CIT, 7-2A-5 NMSA 1978. As the CIT rate is now higher than the top rate in PIT, these filers will also have a higher tax liability. It is assumed that despite a higher income tax liability, the election of entity-level tax is still advantageous over the tax liability impact for Federal Income Tax due to the State and Local Tax (SALT) deduction cap.

[Section 2:] The removal of the word "taxable" in Section 2 of the bill will significantly widen the definition of "engaging in business" and potentially create a nexus in New Mexico for many businesses that currently do not have a reporting requirement, including out-of-state companies. This might increase revenues by adding additional receipts to the gross receipts tax base. There could be a significant increase in the number of taxpayers who have previously filed without taking a credit, deduction, or exemption who now could take this deduction, resulting in a revenue loss for the State and local governments.

Tax & Rev further notes that the economic nexus threshold proposed in this bill has not been tested in court. While the Supreme Court of the United States, in its *Wayfair* decision in 2018 did open the door to economic nexus, that decision did not state with certainty that the threshold of $100,000 of receipts, taxable or otherwise, was constitutionally sound. While almost all states with sales or gross receipts taxes have adopted the $100,000 threshold, some uncertainty remains regarding the permissibility of this threshold. Changing the threshold in New Mexico law could potentially lead to legal challenges, although we regard this outcome as unlikely.

[Section 3:] Businesses may deduct up to $100,000 in any twelve-month period from their gross receipts. Amounts above $100,000 remain subject to GRT. Tax & Rev used data on the monthly number of returns from the RP500 report for the fiscal year 2024 as a proxy for the number of taxpayers. The results from a previous study about New Mexico's Gross Receipts Tax by Ernst & Young, LLP and Georgia State University were employed to determine the percentage of taxpayers that might claim this deduction.[1] Based on this study, Tax & Rev assumed that taxpayers who generate up to $1,000,000 in gross receipts would take the deduction, which implies 93% of taxpayers. The fiscal impact was grown by taking the GRT revenue growth from the December 2024 Consensus Revenue Estimating Group (CREG) forecast and based on the statewide effective GRT rate. The negative impact would be offset at least partly by the restriction of not taking any other GRT credit, deduction, or exemption in the prior year, reducing the cost of existing tax expenditures by an indeterminate amount. The trade-off between the $100,000 deduction and the restriction on taking any other tax benefits will impact the distribution to the local government pursuant to Section 7-1-6.4 NMSA 1978. However, Tax & Rev cannot anticipate whether the effect will be positive or negative on the general fund.

Policy Issues:

[**Section 1:**] Corporations and the economy prefer certainty and that applies to the tax code. Changing the tax code and in this case the tax rates would be the seventh change to the CIT brackets in 11 years as detailed in the table below. The most recent change to a flat rate of 5.9% will only have been in place for one calendar year when the CIT rate increase proposed in this bill takes effect. This uncertainty is seen by corporations as creating a less favorable business environment.

[1] https://www.nmlegis.gov/handouts/RSTP%20062518%20Item%203%20EY%20Tax%20Study%20Final%20Report.pdf

<table>
<tr><th colspan="8">Table 1 – Historical and Current New Mexico CIT rates</th></tr>
<tr><th>Taxable Income</th><th>1987-2013</th><th>2014</th><th>2015</th><th>2016</th><th>2017</th><th>2018-2024</th><th>2025 - present</th></tr>
<tr><td>Up to $500,000</td><td>4.8%</td><td>4.8%</td><td>4.8%</td><td>4.8%</td><td>4.8%</td><td>4.8%</td><td rowspan="3">5.9%</td></tr>
<tr><td>$500,000.01 to $1,000,000</td><td>6.4%</td><td>6.4%</td><td>6.4%</td><td>6.4%</td><td rowspan="2">6.2%</td><td rowspan="2">5.9%</td></tr>
<tr><td>Over $1,000,000</td><td>7.6%</td><td>7.3%</td><td>6.9%</td><td>6.6%</td></tr>
</table>

This bill will create a higher CIT rate (of 6.9%) than the highest marginal personal income tax (PIT) rate of 5.9%. Currently the rates are equal; this bill will automatically increase the tax rate taxpayers electing the entity-level tax, which requires the entity to use the higher of the PIT and CIT rates when electing to pay income tax at the entity level. This creates inequity between businesses, based on the manner in which they organized their business. Many New Mexico businesses are PTEs that do not elect to pay at the entity level, and whose owners pay PIT instead (i.e. the income is passed through to the beneficiaries and taxed under the Income Tax Act), such as LLCs and sole proprietorships. It will be assumed that these taxpayers will expend resources to calculate at the federal and state level the advantages to filing under different entities and under different state tax acts.

CIT is a volatile source of revenue for many states. CIT revenue in New Mexico is notably volatile due to a large share of corporate revenue being tied to oil and natural gas extraction and the volatility of that industry. With new PTE revenue recognized in CIT, the volatility may increase as the new entity-level tax is new and taxpayer preference on how to file is still being observed. In addition, changes at the federal level, including possible changes to the Tax Cuts and Jobs Act of 2017, and its imposition of a SALT cap, could lead to changes at the state level for PTE. The fiscal impact assumes the status quo for PTE filers. But the increase in the rate adds under level of uncertainty in the future behavior of these taxpayers and the impact to revenue. By increasing the rate on all taxpayers though, Section 1 maintains horizontal equity for all taxpayers.

[Section 3:] Tax & Rev considers that this tax incentive will impact mainly small businesses and their customers. As noted below, because businesses cannot deduct taxes which they do not collect from their customers, the primary effect of the bill will be to reduce the cost of goods and services for purchasers, and the economic benefit to the small businesses themselves is indirect, through potentially increased sales, as purchasers who do not have the GRT passed on to them have more money to spend. Nevertheless, even indirect small business tax incentives may help foster growth, increase competitiveness, and provide financial relief.

While allowing small businesses to deduct part of their tax liability in gross receipts can offer benefits, some potential problems or drawbacks can arise. Even though deductions can help reduce tax liabilities, the requirements of this deduction can be complex. Small businesses might struggle to track their monthly deductions to comply with this deduction, especially if they lack dedicated accounting resources. But larger taxpayers with multiple locations can also find it challenging to be in compliance trying to determine when collectively they meet the $100,000 deduction threshold and need to begin charging tax again. This added complexity could increase the time and cost associated with tax filing, increasing their chances of errors or amended tax returns as they learn if this deduction benefits them more than others they have taken. This deduction could create competition between businesses when one is charging tax to customers as usual while another is taking this deduction and not passing tax on to their customers. There is the potential for abuse or manipulation. Some businesses might exploit loopholes, such as continuing to claim exemptions that are not reported to the department. This could result in lost tax revenue for the State and local governments and lead to audits or penalties for businesses that attempt to cheat the system. For legitimate small businesses, this can create an additional burden to prove they comply with the threshold imposed by this deduction. If tax deductions for gross receipts become too intricate, it could lead to a more complicated and less transparent tax system. This would make it harder for small businesses to understand their obligations and for tax authorities to enforce compliance. A more complex

tax system can reduce transparency, make it harder to predict tax outcomes and increase the likelihood of mistakes or misunderstandings by business owners.

There are certain exemptions and deductions from gross receipts tax that a taxpayer will have to choose not to take every other year if they wish to take this deduction that could be difficult for customers. An example of this would be Section 7-9-18.1 NMSA 1978, an exemption for receipts from purchases made with Supplemental Nutrition Assistance Program benefits. This could also affect customers and the distributions for municipal and county governments if a taxpayer chose to skip the deductions under Sections 7-9-92 or 7-9-93 NMSA 1978, which create hold-harmless distributions for local governments. Local governments will not be held harmless if taxpayers claim the $100,000 deduction in this bill instead of the food and medical deductions.

The proposed deduction represents a 4% loss of GRT general fund revenue in FY2026 and FY2027 and loss to local governments revenue. The Section 1 increase to the CIT rate partially offsets the loss to the general fund starting in FY2027. This proposal would decrease recurring general fund revenue by about 1% in FY2026 and less than 0.2% starting in FY2027 due to the offsetting increase in CIT revenue. CIT revenue is a more volatile revenue than GRT revenue and the partial offset in future years may increase or decrease. Local governments do not have an offsetting revenue source proposed in the bill and will lose budgetary flexibility from the loss of one of their primary revenue sources.

Finally, as noted above, the benefit of this deduction should flow mainly to consumers, and not to businesses themselves, because a business cannot pass on GRT to its consumers when it deducts that GRT. The net effect would be to reduce the cost of goods and services to consumers, which may increase consumption and gross receipts overall; but that effect is not clear. Furthermore, consumers may seek out businesses that have not exhausted their deductible amount, in order to receive the benefit of the deduction for themselves. Some businesses may therefore experience decreased sales following exhaustion of the $100,000 amount as consumers seek the same goods from a different retailer who still has capacity to provide GRT relief. The impacts on consumer behavior, and therefore on the economy overall, are hard to predict.

Technical Issues: [Section 3:] Tax & Rev suggests adding additional specification in subsection A, on page 2, on line 21, after the word “exemption” , add “excluding the one for this section” so that lines 19 through 22 read in part: “deducted from the gross receipts of a taxpayer that did not claim a credit, deduction or exemption excluding the one for this section pursuant to the Gross Receipts and Compensating Tax Act in the previous calendar year.” Without this language, taxpayers would only be able to take this deduction every other year.

Tax & Rev suggests in subsection A, page 2, line 19, that “any twelve-month period” be changed to “the calendar year.” It will then read on line 19: “during the calendar year may be deducted . . .” This will bring clarity for taxpayers and Tax & Rev tracking deductions and align the application of both the eligibility on lines 22 and 24 of “engaged in business in each month of the previous calendar year” with claiming deductions then in the following calendar year.

Other Issues: [Section 3:] In subsection A, page 2, lines 20-21: The qualification for a taxpayer to take the deduction is that they did not claim a credit, deduction or exemption in the previous calendar year. Exemptions are not reported to Tax & Rev on GRT tax returns, and therefore Tax & Rev will not be able to determine, in some cases, whether this deduction was properly taken. Furthermore, there are several credits in the GRCTA that have a carryforward provision. It is not clear based on the language provided if using a carryforward from a credit claimed more than a year before would disqualify the taxpayer from taking this new deduction. Where credits may be either refunded or carried forward, this bill may incentivize claiming a refund of the excess credit amount, in order to allow the taxpayer to claim this new

deduction in future years.

Currently, GRT returns may be filed on a monthly, quarterly, or semiannual basis. To determine in subsection A, on page 2, lines 22-24, that a "taxpayer was engaging in business in each month of the previous calendar year" all filings will need to be required as monthly returns only.

Section 3(B) will also be difficult to enforce. Companies may have many reasons to engage in restructuring, and it will be difficult for Tax & Rev to prove that a restructuring was undertaken in order to take advantage of this deduction. That difficulty is compounded by the courts' usual deference to decisions taken by corporate management; so long as there is some reasonable basis for a management decision, the courts will most often support that decision, and not find any improper purpose behind it.

Administrative & Compliance Impact: Tax & Rev will make information system changes and update forms, instructions, and publications. These will be completed during annual tax year implementation.

[Section 2:] The change in "Engaging in Business" will greatly increase the number of taxpayers engaged in business in New Mexico and will increase the number of taxpayers required to register and file GRT returns. Depending on how many more taxpayers would be registering and filing, this may have an impact on operations in Tax & Rev's Audit and Compliance Division (ACD) and Revenue Processing Division (RPD) and the addition of FTE to process these items. In this regard, the non-recurring appropriation of $100,000 might be insufficient to accommodate the volume of taxpayers and submissions of returns to be processed and potential volume of refunds. Further, ACD and the legal services bureau do not have existing resources necessary to ensure taxpayers do not abuse this deduction by artificially splitting into multiple taxpayers to lower receipts; and to address protests that will occur if Tax & Rev attempts to enforce this provision. Tax & Rev's ACD estimates that it will need 1 FTE employee at a pay band 70 to ensure compliance and audit functions on a reoccurring basis.

[Section 3:] Tax & Rev will need to implement a process to confirm the taxpayer qualifies for the deduction by doing a lookback of prior returns and checking for credits and deductions. Exemptions will be impossible to track since they are not claimed on the return. Some taxpayers may be filing for this deduction while taking exemptions, and Tax & Rev does not have a way to review for exemptions. Tax & Rev will also need to implement a process to be able to identify companies who restructure to create subsidiaries for the purpose of the deduction, this will ensure the deduction is only allowed once.

Implementing this bill will have a moderate impact on Tax & Rev's Information Technology Division (ITD), approximately 320 hours or approximately 2 months and about $53,997 in costs ($7,997 of staff workload cost and $46,000 of contractual costs).

Estimated Additional Operating Budget Impact*				**R or NR****	**Fund(s) or Agency Affected**
FY2025	**FY2026**	**FY2027**	**3 Year Total Cost**		
--	$48.5	$96.9	$145.4	R	ACD – FTE
--	$8.0	--	$8.0	NR	ITD - Staff workload costs
--	$46.0	--	$46.0	NR	ITD - Contractual costs

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