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

SPONSOR Dodge **ORIGINAL DATE** 02/12/14 **LAST UPDATED** **HB** 339

SHORT TITLE State Tax Revenues & Local Governments **SB**

ANALYST van Moorsel

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY14	**FY15**	**FY16**	**FY17**	**FY18**		
0.0	($10,000.0)	($10,000.0)	($10,000.0)	($10,000.0)	Recurring	General Fund
See "Fiscal Implications," below.						

Parenthesis ( ) indicate revenue decreases

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY14	FY15	FY16	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
Total		$1,500.0	$1,500.0	$3,000.0	Recurring	TRD

Parenthesis ( ) indicate expenditure decreases

SOURCES OF INFORMATION
LFC Files

Responses Received From
Taxation and Revenue Department (TRD)

SUMMARY

Synopsis of Bill

House Bill amends the Tax Administration Act (TAA) to amend the Taxation and Revenue Department's (TRD) duties and procedures for adjusting distributions to local governments due to over- or underpayments, and provides procedures for counties and municipalities to dispute reductions in distributions.

The bill provides that TRD may adjust the amount of transfer to a municipality or county when information received, whether the information derives from amended returns, approved claims for refund, payments of department-issued assessments, processing of audit adjustments, detection of department error or other source, indicates such an adjustment is appropriate.

The bill provides that ***no adjustment may be made for an overpayment or underpayment of tax prior to the beginning of the calendar year prior to the year of the current month.***

The bill defines a "qualifying amount" as the combined negative amounts attributed to prior periods for a single taxpayer that would be included in computing the aggregate distribution or transfer amount for a local government for the current month. The amounts must exceed both one $100 and 25 percent of the average distribution. Prior to collecting a decrease deemed a qualifying amount in subsequent months, TRD must:

- Reduce the qualifying amount by the sum of any component negative amounts related to periods more than one year prior to the calendar year in which the determination was made plus any positive component amounts related to any periods not more than one year prior to the calendar year in which the determination was made;
- Notify the local government of the reduced qualifying amount TRD will collect beginning in the second month following the month in which notice is given.
- Within 60 days from the date notice is given the local government must either agree to collection of the reduced qualifying amount or protest. If a protest is entered, collection of the reduced qualifying amount shall be deferred or, if already collected, returned until the protest is resolved. If any portion of the reduced qualifying amount is deemed to be due, it may be collected beginning with the next distribution or transfer.
- Decreased distributions pursuant to the State Aid Intercept Act or redirections of distributions to the New Mexico finance authority take precedence over the other adjustments authorized in this section.

HB 339 also provides additional guidance for transfers out of the tax administration suspense fund. At the end of each month, the bill requires certain amounts be retained in the tax administration suspense fund:

- unmatched remittances received within the previous 60 days;
- county business retention GRT pending annual transfer; and
- amounts withheld due to adjustments of distributions or transfers to local governments.

The bill clarifies statute governing respective transfers to municipalities and counties of local option GRT revenue to clarify that the transfer is equal to the net receipts attributable to the local option gross receipts tax imposed by that municipality plus any increases or decreases pursuant to the Tax Administration Act, including a three percent deduction for administrative cost where applicable.

The bill also authorizes TRD to reveal to county or municipality officials the net receipts forming the basis of the distribution or transfer, any adjustment to the transfer, and the proposed calculation of a zero or negative transfer. Information received by a county or municipal official or employee pursuant to Subsection A of this section is return or return information revealed pursuant to a written agreement between the department and the county or municipality and is subject to the provisions of Section 7-1-8 NMSA 1978.

The bill creates a new section of the TAA that allows the municipality or county to dispute an application or proposed application of a qualifying amount by electing to either file an action in district court or to file with the secretary a written protest but not both. The pursuit of one of the remedies constitutes an unconditional waiver to pursue the other.

The effective date of this bill is July 1, 2014.

FISCAL IMPLICATIONS

The Taxation and Revenue Department (TRD) based its analysis of HB 337 on comparing its current practice of allowing reductions to county and municipality distributions based on a three-year lookback to the proposed language limiting negative county distributions only back to January 1 of the prior calendar year. Based on these assumptions, the department estimates the negative impact to the general fund to be at least $10 million per year.

TRD notes this amount could be significantly higher if a large taxpayer reports in the wrong city and the misreporting is not discovered until after the qualifying period. Based on estimates using historical data for negative net receipts distributions/transfers since the beginning of FY 11, if TRD had operated under the provisions of HB 339, it reports the general fund would have absorbed a loss of approximately $30 million in foregone adjustments to local government distributions.

Taxpayers are generally provided a three year period for claiming refunds and these refunds are often quite large. Since local governments would be protected after the first year, the refund would be borne solely by the General Fund.

This bill may be counter to the Legislative Finance Committee (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.

SIGNIFICANT ISSUES

The Taxation and Revenue Department (TRD) has conducted an analysis of limiting negative county distributions only back to January 1 of the prior calendar year as proposed in this bill. The negative impact to the General Fund would be at least $10 million per year. This amount could be significantly higher if a large taxpayer reports in the wrong city and the misreporting is not discovered until after the qualifying period. Based on estimates using historical data for negative net receipts distributions/transfers since the beginning of Fiscal Year 2011, if TRD had operated this way, the General Fund would have eaten approximately $30 million.

New Mexico is a self-reporting state and is therefore reliant on taxpayers to report correctly. TRD provides an administrative service to the counties and municipalities of New Mexico in collecting tax and distributing it to them for which the counties and municipalities pay a fee. The administrative fee to TRD is being reduced from 3.25 percent to 3 percent. As such, TRD contends the state general fund should not be responsible for compensating these counties and municipalities for negative distributions resulting from taxpayer errors, misreporting, refunds, or even fraud.

ADMINISTRATIVE IMPLICATIONS

TRD notes the bill would have a very high administrative impact on its IT Division (ITD), requiring changes to the Revenue Accounting mechanisms for every tax program and CRS distributions to the local governments. Implementation of these changes in GenTax would require contractor resources as the TRD ITD GenTax Bureau does not have sufficient internal developer staff to be able to allocate resources to this project. Since the resources needed to implement this project will have to have expertise in the mechanics of GenTax distributions, this will require a new contract with the software vendor.

The department also projects significant costly impacts to Financial Distribution Bureau (FDB) processes and FTE requirements. TRD identifies the 25 percent threshold for a qualifying event to trigger as the driver behind this administrative impact. In calendar year 2013 alone, there were as many as 500 instances where a distribution was 25 percent greater than the average distribution for a political subdivision; there were as many as 66 instances where a distribution was 25 percent less than the average distribution for a political subdivision.

TECHNICAL ISSUES

TRD notes in its analysis of the bill that limiting the qualifying period to one year impedes TRD's ability to carry out responsibilities under limitation on assessment as outlined in Section 7-1-18 NMSA 1978. It also impedes TRD's ability to make refunds or credits as outlined in Section 7-1-29 NMSA 1978, and in disputing liabilities; claim for credit, rebate or refund as outlined in Section 7-1-26 NMSA 1978:

> D. Except as otherwise provided in Subsection E of this section, no credit or refund of any amount may be allowed or made to any person unless as the result of a claim made by that person as provided in this section:
>
> (1) within three years of the end of the calendar year in which:
>
> (a) the payment was originally due or the overpayment resulted from an assessment by the department pursuant to Section 7-1-17 NMSA 1978, whichever is later;…

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

PvM/jl