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

		ORIGINAL DATE	02/07/14		
SPONSOR	Beffort	**LAST UPDATED**	02/14/14	**HB**	
SHORT TITLE	Software Development Gross Receipts			**SB**	175/aSFC
				ANALYST	van Moorsel

REVENUE (dollars in thousands)

Estimated Revenue					**Recurring or Nonrecurring**	**Fund Affected**
FY14	**FY15**	**FY16**	**FY17**	**FY18**		
	(<$50.0)	(<$50.0)	(<$50.0)	(<$50.0)	Recurring	General Fund

(Parenthesis ( ) Indicate Revenue Decreases)

SOURCES OF INFORMATION
LFC Files

Responses Received From
Taxation and Revenue Department (TRD)

SUMMARY

Synopsis of SFC Amendment

The Senate Finance Committee amendment to Senate Bill 175 changes the definition of "eligible software development company" to specify it must have established its primary business in New Mexico after July 1, 2014, rather than July 1, 2002. The amendment makes the deduction eligible to new businesses, and would thus reduce the fiscal impact.

Synopsis of Original Bill

Senate Bill 175 expands the definition of "software development services" for purposes of a deduction from gross receipts. The bill defines "software development services" as design, development, programming, testing or the deployment of nontangible custom software or customized adaptation of commercially available software for data processing applications, software integration, digital imaging, digital design, graphics, electronic messaging, mobile applications, web sites, graphical user interfaces, artificial intelligence or data storage and retrieval. "Software development services" does not include training and computer support services.

The "eligible software development company" is amended to specify it must have established its primary business in New Mexico after July 1, 2002.

The bill includes a reporting requirement. A taxpayer allowed the deduction pursuant to this section must report the amount of the deduction separately, and the Taxation and Revenue Department (TRD) must compile these taxpayer reports annually. Every three years, beginning in 2017, TRD must compile and report the annual reports to the Revenue Stabilization and Tax Policy Committee and the LFC with an analysis of the deduction.

The effective date of the provisions of the bill is July 1, 2014.

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. 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.

The Taxation and Revenue Department notes most of the categories added to the definition of software development are probably already covered under the current definition without being specified separately. However, including website development could cause a substantial increase in the deduction. Classification data is not available at a significantly detailed level to distinguish between similar businesses that may or may not be eligible.

In FY2013, taxpayers classified as custom computer programming services, which includes all of the listed types of taxpayers as well as some others, reported taxable gross receipts of about $15.9 million out of total gross receipts of $29.7 million. Because the current deduction is not reported separately, there is no way to directly measure how much of the deducted gross receipts are deducted due to Section 7-9-57.2 NMSA 1978 and not some other section. Assuming that 50 percent of current taxable gross receipts would become newly available under this bill, the state would forego about $480 thousand in gross receipts revenue. The figure is assumed to grow at the UNM Bureau of Business and Economic Research forecast rate of employment growth in professional and technical services, the broader category that includes software development.

*Note: If a greater portion of the gross receipts are attributable to website development, the fiscal impact could be significantly greater.

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.

TECHNICAL ISSUES

This bill does not contain a sunset date. The LFC recommends adding a sunset date.

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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