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

SPONSOR McCamley **ORIGINAL DATE LAST UPDATED** 1/27/15 **HB** 16

SHORT TITLE Surtax on Certain Corporations **SB**

ANALYST van Moorsel

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY15	FY16	FY17	FY18	FY19		
	$0.0 - $6,000.0	$0.0 - $15,000.0	$0.0 – $13,000.0	$0.0 - $11,000.0	Recurring	General Fund

(Parenthesis ( ) indicate revenue decreases

SOURCES OF INFORMATION
LFC Files

Responses Received From
Taxation and Revenue Department (TRD)
Department of Finance and Administration (DFA)

SUMMARY

Synopsis of Bill

House bill 16 creates a new section of the Corporate Income and Franchise Tax Act to impose a 1.0 percent surtax on the net income of domestic and foreign corporations that pay their chief executive officers or similar senior executive a salary that is at least 100 times greater than the average salary of all other employees not in upper management.

The provisions of HB 16 apply to taxable years beginning on or after January 1, 2015.

FISCAL IMPLICATIONS

To estimate the impact of HB16, TRD calculated the average ratio of CEO compensation of Russell 3000 companies to New Mexico average worker's pay. The national average pay for a CEO is about $5,345,418 whereas New Mexico average worker's pay is about $36,536, for a ratio of 146. This implies that, on average, companies pay CEOs about 146 times what the average New Mexico worker is paid. Next, TRD assumed the top 50 CIT filers would be most likely to compensate CEOs or upper management at least 100 times more than the average compensation of all other employees. Applying the 1 percent surtax against the net income apportioned to New Mexico by these taxpayers yields an average of $11 million in revenues. If implemented, the proposed legislation would increase corporate income taxes by about one percent for any qualifying company. FY16 is a partial year impact as the applicable date is January 1, 2015, and the taxes will not be reported until the following year.

SIGNIFICANT ISSUES

As DFA notes in its analysis, this bill aims to address growing concern over extravagant CEO salaries and bonuses. DFA adds the provision is similar to the requirements of the federal Dodd-Frank Act, which requires corporations to disclose to the Securities and Exchange Commission the CEO/worker pay ratio. In May 2014 the California Senate narrowly rejected a bill that attempted to tie corporate tax rates to CEO/worker pay ratios. The bill received formal opposition from 19 businesses and business associations and support from only the California Labor Federation.

DFA adds that the bill may have the unintended consequence of causing publicly traded companies and financial institutions to depart New Mexico. Further, the bill's provisions may disproportionately affect retail companies with a large number of entry-level sales personnel that would drive up the CEO/worker pay ratio.

DFA's analysis also cites the AFL-CIO, in reporting the CEOs of the S&P 500 Index made 354 times the average worker salary in 2012.

ADMINISTRATIVE IMPLICATIONS

TRD reports the provisions of the bill would have a an administrative impact on the department requiring approximately 400 hours to modify the CIT returns to require information about CEO or other executive staff compensation as well as average compensation for other employees.

TRD adds that, to administer the CIT surtax properly, the department would need to make definitions and regulations, noting the current definitions of chief executive officer, corporate officer, executive salaries, upper management and salaries are vague and subjective. TRD adds that without good, easy-to-administer definitions for these terms, it could be required to commit additional resources toward validating and reviewing returns to ensure compliance.

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL

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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