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

SPONSOR Stewart **ORIGINAL DATE** 2/1/16 **LAST UPDATED** **HB**

SHORT TITLE Delay Corporate Income Tax Rate Reduction **SB** 90

ANALYST Graeser

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY16	**FY17**	**FY18**	**FY19**	**FY20**		
$2,800.0	$14,100.0	$10,700.0	$0.0	$0.0	Nonrecurring	General Fund

Parenthesis ( ) indicate revenue decreases

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY16	FY17	FY18	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
Total	$14.0	$0.0	$0.0	$14.0	Nonrecurring	TRD Operating

Parenthesis ( ) indicate expenditure decreases

SOURCES OF INFORMATION
LFC Files

Responses Received From
Taxation and Revenue Department (TRD)

SUMMARY

Synopsis of Bill

Senate Bill 90 delays the implementation of the corporate income tax (CIT) reduction in TY2017. Under existing law (Laws 2013, Chapter 160 – CS HB 641), the top CIT rate is reduced from 7.3% to 6.9% in TY15 and from 6.9% to 6.6% in TY16 (see first chart in Fiscal Impact section). This bill proposes to delay the TY16 top CIT rate reduction to TY17 and all subsequent rate reductions by one year.

There is no effective date of this bill. It is assumed that the new effective date is 90 days after this session ends (May 18, 2016). This effective date is after the due date for the first quarter estimated payment for calendar year 2016 taxpayers.

FISCAL IMPLICATIONS

The delay in rate reductions will impact three quarters of the estimated payment in TY16 and one-quarter of the estimated payment in FY16. The delay in the rate reduction will partially impact FY16 and have a full impact on FY17 and FY18 and no impact after that. To determine the fiscal impact on the General Fund, TRD analyzed the difference between the previously estimated impact (see second chart in Fiscal Impact section of the rate reduction and shifting those impacts by one year. These percentage changes were applied to the January 2016 consensus General Fund revenue estimate.

Laws 2013, Chapter 160 also provided for a phased in single sales factor for manufacturers and mandatory combined filing for some other taxpayers. Delaying the rate reduction but not delaying the single sales factor phase-in makes the analysis somewhat difficult. To a first order approximation, Chart 2 is appropriate. To a second order, however, the single sales phase-in will be more expensive to the general fund for each year until fully phased in.

<table>
<tr><th colspan="7">CHART 1: Current Law Rate Reductions</th></tr>
<tr><th></th><th>TY2013</th><th>TY2014</th><th>TY2015</th><th>TY2016</th><th>TY2017</th><th>TY2018</th></tr>
<tr><td>Income < $500k</td><td colspan="6">4.8%</td></tr>
<tr><td>Income $500k - $1m</td><td colspan="4">6.4%</td><td rowspan="2">6.2%</td><td rowspan="2">5.9%</td></tr>
<tr><td>Income > $1m</td><td>7.6%</td><td>7.3%</td><td>6.9%</td><td>6.6%</td></tr>
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<table>
<tr><th colspan="8">CHART 2: Fiscal Impact of Rate Reduction</th></tr>
<tr><th colspan="8">Updated Impact Analysis Presented to RSTP in September 2015</th></tr>
<tr><th>Percentage impact of rate reduction</th><th>FY14</th><th>FY15</th><th>FY16</th><th>FY17</th><th>FY18</th><th>FY19</th><th>FY20</th></tr>
<tr><td>Current law impact</td><td>-3%</td><td>-7%</td><td>-10%</td><td>-14%</td><td>-17%</td><td>-17%</td><td>-17%</td></tr>
<tr><td>Proposed law impact</td><td>-3%</td><td>-7%</td><td>-10%</td><td>-10%</td><td>-14%</td><td>-17%</td><td>-17%</td></tr>
</table>

The greatest difficulty with analyzing these corporate income tax bills is the long latency between the beginning of the tax year and the receipt, processing and compilation of data. For example, TY 2013 calendar year taxpayers filed their first quarter estimate in April 2013, an extension of time to file in March 2014, filed final returns in September 2014, with final compilation and summary not available until April 2015.

This bill is one link in a chain to rethink past reductions in revenues, most of which were enacted to make the state’s tax environment more attractive for corporations. Each of the FIRs for tax expenditure or rate reduction bills were published with the following warning:

“This bill 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.”

The current oil and natural gas based reduction in appropriable revenues gives new meaning to the past LFC warnings on the subject of adequacy.

SIGNIFICANT ISSUES

7-2A-9.1 NMSA 1978 provides as follows: "Estimated payments are due the fifteenth day of the fourth month of the taxable year, the fifteenth day of the sixth month of the taxable year, the fifteenth day of the ninth month of the taxable year and the fifteenth day of the twelfth month of the taxable year."

For calendar year taxpayers, the first quarter estimate is due on April 15, the second quarter on June 15. The FY 16 impact shown in the table is at least partially voluntary, since most corporate taxpayers use the "safe harbor" method of

TRD notes that this bill implicates policy principles of adequacy and efficiency. By delaying the rate reduction, the bill should increase revenue for three fiscal years because each of these fiscal years contains all or portions of tax years effected by the delayed reduction. However, CIT rates were reduced in order to keep New Mexico competitive with other states in terms of economic development. The impact of the delayed deduction, in terms of economic development is unknown.

ADMINISTRATIVE IMPLICATIONS

TRD reports minimal impact:
Other Issues: Low IT impact (200 hours) – Requires changes to GenTax tax rate configuration for corporate income tax program.

Administrative & Compliance Impact: Minimal impact. The costs of modifying the forms and instructions, publications, backend systems and electronic filing systems for the corporate income taxes can be absorbed with the annual renewal of the tax program. No impact to financial distribution business processes.

TECHNICAL ISSUES

If passed without an emergency clause, the first quarter estimate for calendar year 2016 taxpayers is due before the effective date of the legislation. It is uncertain how the safe harbor rules would apply. To avoid litigation, it might be appropriate to suspend the estimated payment penalty provisions for the year of the delay.

ALTERNATIVES

2013's HB-641 was built from a number of constituent bills, including HTRC CS for HB-182 and 507. This committee substitute made the CIT rate reduction contingent on meeting a 7% general fund reserve target and gave authority to the DFA secretary to administratively delay the CIT rate reduction to maintain solvency. If that contingency feature had been included in the the final version of HB-641's rate reductions, the current bill would not have been necessary.

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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