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

ORIGINAL DATE 03/02/17
SPONSOR Burt **LAST UPDATED** **HB**

SHORT TITLE Military Base Construction Gross Receipts **SB** 485

ANALYST Clark

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY17	**FY18**	**FY19**	**FY20**	**FY21**		
$0	Indeterminate but Negative				Recurring	General Fund
$0	Indeterminate but Negative				Recurring	Local Governments

Parenthesis ( ) indicate revenue decreases

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY17	FY18	FY19	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
Total	$28.0	$0	$0	$28.0	Nonrecurring	Taxation and Revenue Department

Parenthesis ( ) indicate expenditure decreases

SOURCES OF INFORMATION
LFC Files

Responses Received From
Taxation and Revenue Department (TRD)
Office of Military Base Planning and Support (OMBPS)

SUMMARY

Synopsis of Bill

Senate Bill 485 adds a new Section to the Gross Receipts and Compensating Tax Act to allow for a deduction from the gross receipts tax (GRT) for receipts from the sale of services for construction of infrastructure on a military base to support training missions involving F-16 tactical fighter jets in the state.

There is no effective date of this bill, and it is assumed that the effective date is 90 days after this session ends, but the bill specifies the deduction may only be taken in FY18 – FY22.

FISCAL IMPLICATIONS

This bill is impossible to score. The Taxation and Revenue Department (TRD) and LFC do not have access to any publically available information from the Department of Defense (DOD) or the U.S. Air Force (USAF) that would enable the agencies to estimate planned or possible future construction costs related to F-16 training missions and thus estimate the fiscal impact of the proposed deduction. However, it appears at this time the bill would only apply to Holloman Air Force Base near Alamogordo.

If the deduction fulfills its purpose and plays a key role in bringing F-16 training missions to the state that would not have come but for this deduction, the state benefits overall and there is no loss of revenue. However, any GRT revenue the state would otherwise receive from such construction projects that are already planned or would occur in the future without this deduction would represent a net loss to the state and local governments. Without any data to unequivocally state no such construction would occur absent this incentive, it must be scored as a negative impact.

This bill would set a precedent for creating deductions for some taxable services on military bases and could open the door for additional deductions in the future, further eroding the state's tax base. LFC and tax experts have noted over the years such erosion leads to higher GRT rates and more revenue volatility.

This bill may be counter to the LFC tax policy principles 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.

SIGNIFICANT ISSUES

New Mexico benefits significantly from its military installations in terms of revenue to state and local governments, employment, and intellectual capital related to research and development work. As with private companies, New Mexico is often in competition with other states for military projects that would bring additional investment and jobs. However, there is mixed economic data and studies showing the effectiveness, or lack thereof, of tax incentives to impact long-term economic growth.

TRD and the Office of Military Base Planning and Support (OMBPS) provided the following analysis.

The USAF recently selected Holloman Air Force Base (HAFB) as a base to establish two additional F-16 training squadrons. HAFB's selection is considered as an "interim-basing decision" meaning the USAF will perform a more expansive analysis of 34 candidate bases (including HAFB) in order to select the permanent base for the F-16 aircrafts.

The USAF considered three other bases in addition to HAFB in deciding the site for the interim base—two in Arizona (Luke AFB and Tucson International Airport) and one in Texas (Joint Air Base San Antonio – Kelly). While HAFB was ultimately the winner in the interim selection process, the USAF analysis graded HAFB as 'yellow' for Area-Cost-Factor (ACF). ACF is a performance-cost measure used in DOD publications, based on regional market conditions that are updated every year. To understand ACF for instance, the nationwide cost factor is 1.0 while HAFB's cost factor is 0.99; this means HAFB's main competition is Joint Air Base San Antonio – Kelly where the ACF is 0.86 as there are no gross receipts costs for construction services in Texas.

The Air Force's analysis noted that HAFB's facility and infrastructure has the capacity to successfully support the F-16 mission and is well suited for this type of program. However, some hangars and other buildings will require some renovation for continued long term use. As the Air Force begins its analysis on the permanent basing, it's important that New Mexico establish the conditions to make HAFB as competitive as possible or risks losing this program to another state.

Conversely, the potential benefits of the proposed deduction are very difficult to estimate, regardless of the absence of hard data regarding the estimated costs of construction at HAFB. Because New Mexico will not be collecting any tax revenue through income taxes for active service members or through the service and repair of aircraft or fuel sale that are exempt from the gross receipts tax, the potential break-even point to the state from enacting the proposed deduction is difficult to discern.

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.

ADMINISTRATIVE IMPLICATIONS

TRD reports implementing the bill would cause a low impact on TRD's Information Technology Division (ITD) of approximately 400 work hours with an annual cost of $28 thousand. ITD assesses the bill does not provide for adequate time to complete all required system changes in order to incorporate the proposed deduction by the implementation deadline of June 16, 2017.

OTHER SUBSTANTIVE ISSUES

TRD provided the following additional analysis.

The bill requires that deductions taken are separately reported in a manner required by the department. The department would need to determine the manner in which taxpayers will be required to report the proposed deduction, to comply with Section 1 D. Changes to the department's general accounting system (GenTax) would need to be made to allow for this new deduction.

The proposed deduction could be subject to the financial statement disclosure requirements per GASB Statement No. 77. If that is the case, an assessment of the deduction against the tax abatement criteria specified in GASB 77 would need to be performed to determine if the deduction meets the criteria. If so, then disclosure would need to be made in the department's notes to its financial statements.

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

Does the bill meet the Legislative Finance Committee tax expenditure policy principles?

1. **Vetted**: The proposed new or expanded tax expenditure was vetted through interim legislative committees, such as LFC and the Revenue Stabilization and Tax Policy Committee, to review fiscal, legal, and general policy parameters.
2. **Targeted**: The tax expenditure has a clearly stated purpose, long-term goals, and measurable annual targets designed to mark progress toward the goals.
3. **Transparent**: The tax expenditure requires at least annual reporting by the recipients, the Taxation and Revenue Department, and other relevant agencies.
4. **Accountable**: The required reporting allows for analysis by members of the public to determine progress toward annual targets and determination of effectiveness and efficiency. The tax expenditure is set to expire unless legislative action is taken to review the tax expenditure and extend the expiration date.
5. **Effective**: The tax expenditure fulfills the stated purpose. If the tax expenditure is designed to alter behavior – for example, economic development incentives intended to increase economic growth – there are indicators the recipients would not have performed the desired actions "but for" the existence of the tax expenditure.
6. **Efficient:** The tax expenditure is the most cost-effective way to achieve the desired results.

LFC Tax Expenditure Policy Principle	Met?	Comments
Vetted	✘	
Targeted		
Clearly stated purpose	✓	
Long-term goals	✘	
Measurable targets	✘	
Transparent	✓	
Accountable		
Public analysis	?	
Expiration date	✓	
Effective		
Fulfills stated purpose	?	
Passes "but for" test	?	
Efficient	?	
Key: ✓ Met ✘ Not Met ? Unclear		

JC/sb