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

ORIGINAL DATE 2/7/18
SPONSOR SCORC **LAST UPDATED** ____ **HB** ____

SHORT TITLE Tax Code Cleanup & Reporting **SB** 128/SCORCS

ANALYST Clark

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY18	**FY19**	**FY20**	**FY21**	**FY22**		
None	Minimal but Likely Positive; Helps Preserve Existing Revenues				Recurring	General Fund, Local Governments

Parenthesis ( ) indicate revenue decreases

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY18	FY19	FY20	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
Total		Minimal	Minimal	Minimal	Recurring	TRD Operating Budget

Parenthesis ( ) indicate expenditure decreases

Conflicts (regarding insurance “in lieu of” language) with SB68, SB162, and SB175

SOURCES OF INFORMATION
LFC Files

Responses Received From (on similar provisions in other bills)
Taxation and Revenue Department (TRD)
New Mexico Municipal League (NMML)
Office of Superintendent of Insurance (OSI)
Economic Development Department (EDD)

SUMMARY

Synopsis of Bill

The Senate Corporations and Transportation Committee Substitute for Senate Bill 128 performs various tax code cleanup and reporting functions. It removes a potential loophole in the insurance “in lieu of” provision, where the possibility exists for taxpayers in the future to merge with an insurance company or begin selling insurance policies to avoid nearly all other taxes,

including gross receipts tax (GRT). It also narrows a GRT deduction for the sale of chemicals and reagents to prevent the sort of attempted exploitation of the deduction the state has seen over the last two years, resulting in taxpayer protests of about $165 million for this one deduction. However, while the deduction is narrowed to prevent exploitation and possible significant loss of state revenues, the intent is to leave the deduction intact for the oil and gas and mining industries for all the uses for which the deduction was intended and the industries have historically used it.

The bill also requires separate reporting for several deductions (many other deductions already require this).

Finally, the bill repeals a variety of tax expenditures that are expired or unused.

The effective date of this bill is July 1, 2018.

FISCAL IMPLICATIONS

While the bill would likely generate minimal revenue gains compared with the forecast, it has the potential to protect existing state revenues. For example, amending the insurance "in lieu of" provision and the related GRT exemption could potentially save many tens or hundreds of millions of dollars if taxpayers attempt to exploit the existing tax code in the future.

The $165 million tied up in protests regarding the chemicals and reagents deduction is a matter that will need to be resolved by the Administrative Hearings Office and the courts; however, this cleanup legislation could help protect future revenues in the tens or hundreds of millions of dollars.

The other provisions of the bill would likely generate no revenue but would remove expired or unused tax expenditures from statute.

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

Legislative staff and others worked to carefully craft the revised insurance "in lieu of" provisions to remove (to a large degree) a potential loophole in the tax code while not impacting any of the insurance companies and others who currently validly use this tax exclusion. The exclusion was created so that these entities would be taxed under the premium tax, health insurance premium surtax, and fees contained within the Insurance Code and not taxed through any other means except for property taxes and, for insurance companies, corporate income taxes. Through discussion with industry, it does not appear this change would adversely impact them, and while it may not remove all possible ways to exploit this tax exclusion, it significantly reduces that possibility.

The intent was similar for narrowing the chemicals and reagents deduction. A significant number of oil, gas, and mining company officials, accountants, attorneys, other industry representatives, and tax professionals, recently met with legislative and executive staff to discuss the deduction. The discussion was useful and productive overall, but no decisions regarding statutory language changes were made during the meeting. The language in the bill is the result of an attempt to protect the oil and gas and mining industries while narrowing provisions to exclude known or suspected forms of attempted exploitation leading to the $165 million backlog of protests after the Taxation and Revenue Department deemed certain deduction claims invalid. Additional information from these industries on how to word the amended language to avoid unintentional impacts would be extremely useful.

The New Mexico Municipal League (NMML) reports that by collecting and reporting data individually on certain deductions, estimates of the impact of potential tax reform will be more precise. Separate reporting for many deductions has potential to improve revenue tracking and forecasting and significantly improve the ability to score future tax reform proposals.

Many deductions do not require separate reporting by taxpayers and are lumped together in a single dollar amount on the forms submitted to TRD. Combined reporting of deductions leads to either nonexistent or imprecise cost estimates and complicates any possible cost-benefit analyses. Separate reporting of these costs would solve half the problem of performing such analyses. Additionally, separate reporting of some deductions with likely very large fiscal impacts could significantly improve analysis of tax reform proposals by reducing the number of unknown variables.

Separately Reported Deductions	
7-9-54.3	Wind and solar generation equipment sales to governments
7-9-56.2	Hosting world wide websites
7-9-57.2	Sale of software development services
7-9-63	Publication sales
7-9-64	Newspaper sales
7-9-65	Chemicals and reagents
7-9-73.1	Hospitals
7-9-73.2	Prescription drugs
7-9-83	Jet fuel (GRT)
7-9-84	Jet fuel (comp)
7-9-86	Sales to film production companies
7-9-108	Management or investment advisory services for mutual funds, hedge funds, or REITs

Repeals	
7-2-18.4	Business facility rehabilitation credit (PIT)
7-2-18.5	Welfare-to-work credit
7-2-18.8	Certain electronic equipment credit
7-2-18.21	Blended biodiesel fuel credit (PIT)
7-2-18.27	Physician participation in cancer treatment credit
7-2A-15	Business facility rehabilitation credit (CIT)
7-2A-23	Blended biodiesel fuel credit (CIT)
7-2D-1 thru 7-2D-14	Venture capital investments credit
7-9-106	Military construction services

ADMINISTRATIVE IMPLICATIONS

TRD will likely report there will be a minimal, nonrecurring impact to make changes to GenTax and reporting forms and a very minimal, recurring impact due to the additional annual reporting requirements.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

The bill conflicts (regarding the insurance "in lieu of" language) with SB68, SB162, and SB175. It conflicts with SB68's repeal of 7-9-65 NMSA 1978, which is amended in this bill and in an identical manner in HB206.

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.

JC/al