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FISCAL IMPACT REPORT

		LAST UPDATED	2/1/24
SPONSOR	Sen. Wirth/Rep. Cadena	**ORIGINAL DATE**	1/31/24
SHORT TITLE	Corporate Income Tax Liability	**BILL NUMBER**	Senate Bill 181
		ANALYST	Gray

REVENUE*
(dollars in thousands)

Type	FY24	FY25	FY26	FY27	FY28	Recurring or Nonrecurring	Fund Affected
CIT			\$1,000.0 to \$1,700.0	\$1,100.0 to \$1,700.0	\$1,100.0 to \$1,800.0	Recurring	General Fund

Parentheses ( ) indicate revenue decreases.
*Amounts reflect most recent analysis of this legislation.

Sources of Information

LFC Files

Agency Analysis Received From
Economic Development Department (EDD)
Taxation and Revenue Department (TRD)

Agency Analysis was Solicited but Not Received From
Department of Finance and Administration (DFA)

SUMMARY

Synopsis of Senate Bill 181

Senate Bill 181 amends the Corporate Income Tax Act to add "subpart F" into the corporate income tax (CIT) taxable base and modifies which filers can file as a water's-edge group.

Subpart F income is defined by the Internal Revenue Code (IRC) as relating to controlled foreign corporation's:

- insurance income,
- base company income,
- illegal bribes, and
- the income derived from certain foreign countries.

The provisions of the bill apply to taxable years beginning on or after January 1, 2025.

FISCAL IMPLICATIONS

The revenue impact was estimated by the Taxation and Revenue Department (TRD) using tax return data from fiscal years 2021 to 2023. The agency notes:

> CIT is an extremely challenging revenue to forecast in times of relative stability. Given the variable economic conditions that may impact CIT taxpayers, the estimate has been presented as a positive range to emphasize the uncertainty of the magnitude of the impact. Using the December 2023 Consensus Revenue Estimating Group (CREG) forecast, the average range impact is grown by the current growth rate for gross CIT.

SIGNIFICANT ISSUES

TRD analysis notes that subpart F of the IRC was enacted in 1960s to prevent the deferral of taxation on certain income types of controlled foreign corporations. The agency notes:

> A foreign corporation is a CFC if more than 50 percent of either: (1) the total combined voting power of all classes of stock entitled to vote, or (2) the total value of the stock of such corporation, is owned by United States shareholders on any day during the foreign corporation's taxable year. IRC Section 957(a). Prior to the enactment of Subpart F, a CFC's income was not taxable income of its U.S. shareholders until it was distributed to them, usually in the form of a dividend. Corporations were incentivized to earn and hold income in low- or no-tax foreign jurisdictions to defer taxation of their income as long as possible. Shareholders used various methods, most often loans from the CFC, to access the income without paying tax. The U.S. Congress responded by enacting Subpart F, which requires U.S. shareholders to include some CFC income in their taxable income, whether or not it was actually distributed. The rules regarding calculation of Subpart F income are very complicated, and subject to extensive regulation by the U.S. Department of the Treasury. Subpart F income forms approximately 2.3 percent of federally taxable corporate income.

Until 2019, New Mexico included subpart F income in "base income". The federal Tax Cuts and Jobs Act of 2017 (TCJA) made further changes to the calculation of corporate taxable income by addressing the off-shoring of a different type of income, primarily derived from the sale of intangible property. This income is called "global intangible low taxed income", or "GILTI".

TRD further notes:

> As part of the legislative changes enacting "water's edge" reporting that were made in the 2019 Session, the requirement to include Subpart F income in taxable income was removed from statute. Such change was also in response to a "transition tax" included in the TCJA, which temporarily expanded the amount of Subpart F income that would be included in shareholder income. However, this removal was not legally required. As New Mexico generally conforms to federal tax law, it is therefore consistent with that conformity, and with sound tax policy generally, to put Subpart F income back into the corporate income tax base. The second change made by the bill is to the definition of "water's edge group". Current law excludes from the water's edge group all corporations, no matter where organized or incorporated, that have less than 20 percent of their property, payroll, and sales sourced to the United States under the sourcing rules of the Uniform Division of Income for Tax Purposes Act, Section 7-4-1 et seq., NMSA 1978.

> The bill eliminates this exclusion for corporations organized or incorporated in the United States; all such corporations will be included in the water's edge group, no matter how much of their property, payroll, and sales are sourced to the United States. This change conforms to federal law and relevant case law describing the boundaries of states' power to tax income not sourced to the United States, and furthers federal policy of preventing corporate tax deferral by shifting income to foreign sourcing.

The agency also writes that many taxpayers and tax practitioners have inquired about Section 250 in the current definition of base income. "Changing the language to "less the amount deducted pursuant to Section 250" makes clear that Section 951A income less the Global Intangible Low Tax Income (GILTI) deduction provided for in Section 250, is excluded from taxable income."

BG/al/ne