



**Georgia State University  
Roundtable Discussion  
Expansion of Sales Tax Base to Services  
October 30, 2007**

## **New Mexico's Gross Receipts Tax on Services**

### **Background**

New Mexico's Gross Receipts Tax ("GRT") is a hybrid of a retail sales tax and a gross receipts tax. The tax is defined as a privilege tax on all receipts from sale or lease of property (including some types of intangible property) and sale of services. Exemptions are provided for transactions taxed under other taxes and for sales by governments and non-profits. Deductions serve a variety of purposes, including limiting the double taxation of goods or services under the GRT itself.

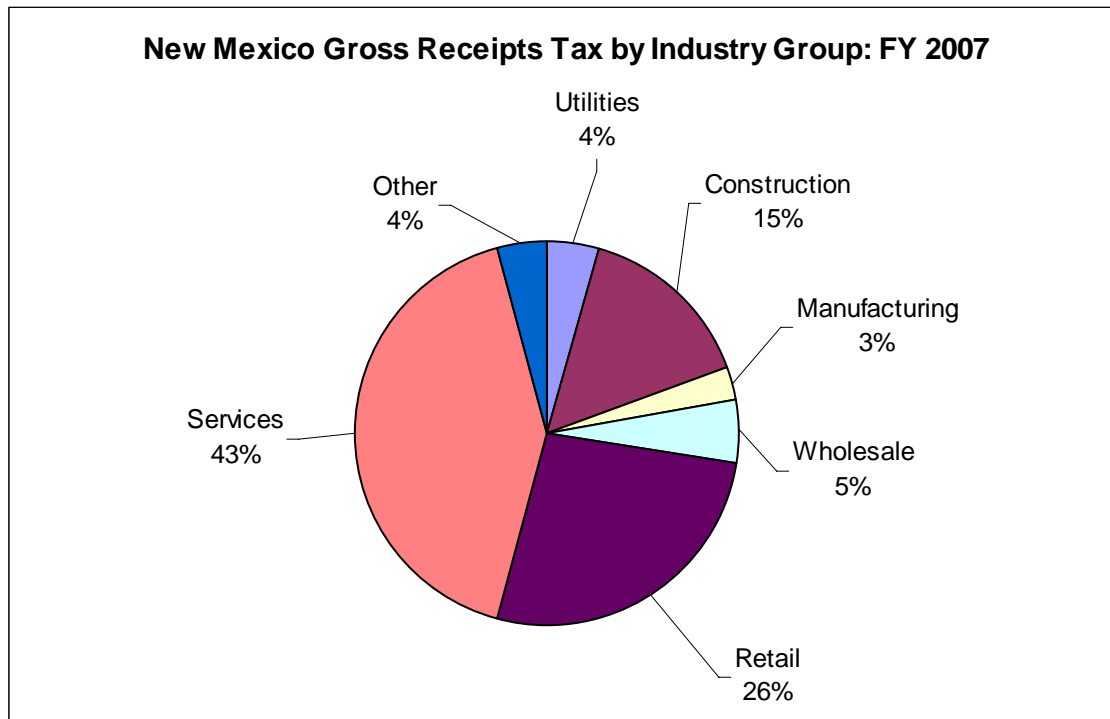
A tax on gross revenue of virtually all businesses in the state was initially imposed in 1935. The Gross Receipts and Compensating Tax was codified in its current form in 1966 at a statewide rate of 3 percent. The statewide rate was increased several times, reaching the current level of 5% in 1990. Local governments have been authorized to impose additional taxes, some of which require voter approval. Tax rates authorized now total about 3% for cities and an additional 3% for counties, making the maximum possible imposition under present law about 11%. The highest combined local tax rate imposed is currently 2.875%, for a combined maximum state and local rate of 7.875%.

In FY 2007, state and local GRT revenue was \$3.2 billion on a base of \$48.3 billion, for an average statewide effective tax rate of 6.6%. For purposes of comparing that base, total Personal Income in FY 2007 was approximately \$60 billion, and total Gross State Product was \$71.4 billion. A total of 60% of GRT revenue went to State funds, mostly to the General Fund, while the other 40% went to Local Governments, mostly to Cities.

## Role of Services in the GRT Base

As illustrated in Figure 1, Services broadly defined comprise 43% of the GRT tax base, easily the single largest component of the GRT base. Retail and Wholesale Trade comprise 32%, while the other major component is Construction at 15%.

**Figure 1**

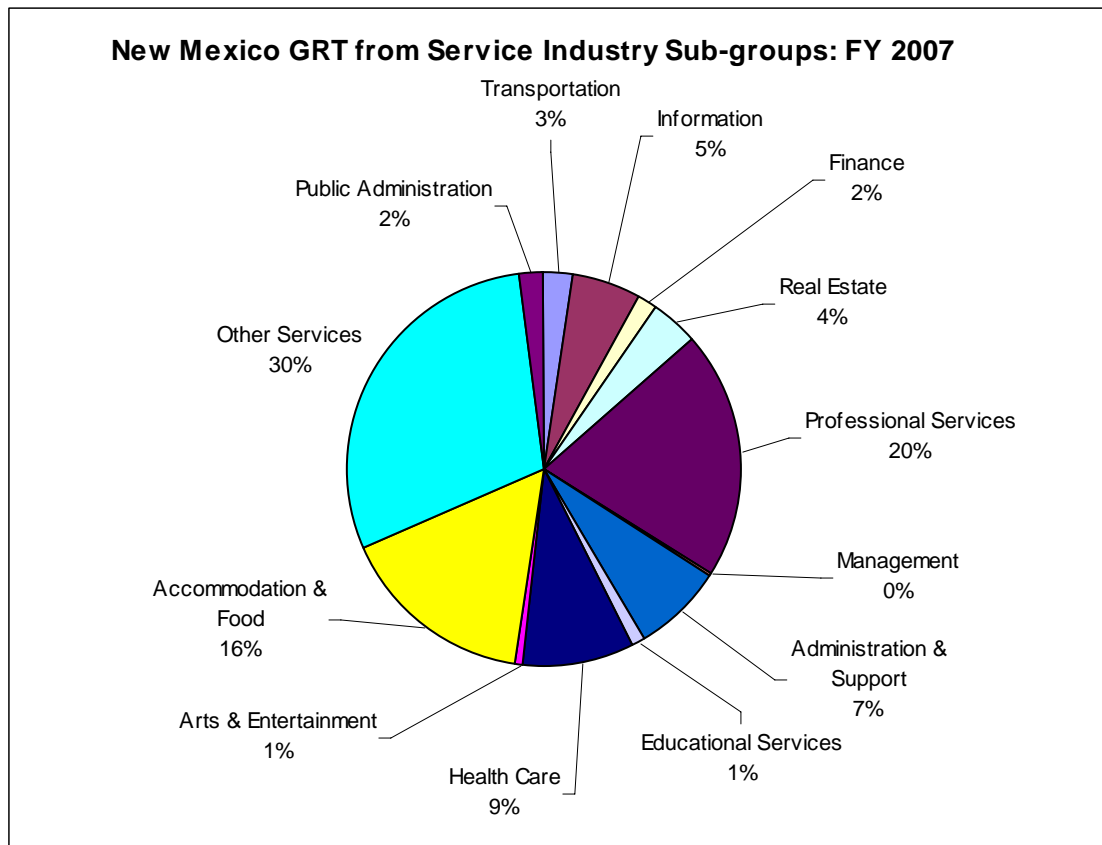


Source: N.M. Taxation and Revenue Department, RP-80 Analysis of Gross Receipts Tax by Industry

## GRT Base Attributable to Service Industry Sub-Groups

Figure 2 shows some details on the share of Service industry GRT attributable to different sub-sectors. Professional Services and Accommodation/Food are two of the largest subgroups. The former reflects the large role of federally-sponsored R&D in the state's economy, while the latter reflects the significant role of tourism. The large share attributable to "Other Services" is partly a reflection of the weakness of the classification system used for processing tax returns. Industry groups are self-reported by taxpayers, and are only reviewed by the Department on audit. Most Personal Services as well as Repair Services are included in the "Other Services" category. Data supporting Figures 1 & 2 is presented in Table 1.

**Figure 2**



Source: N.M. Taxation and Revenue Department, RP-80 Analysis of Gross Receipts Tax by Industry

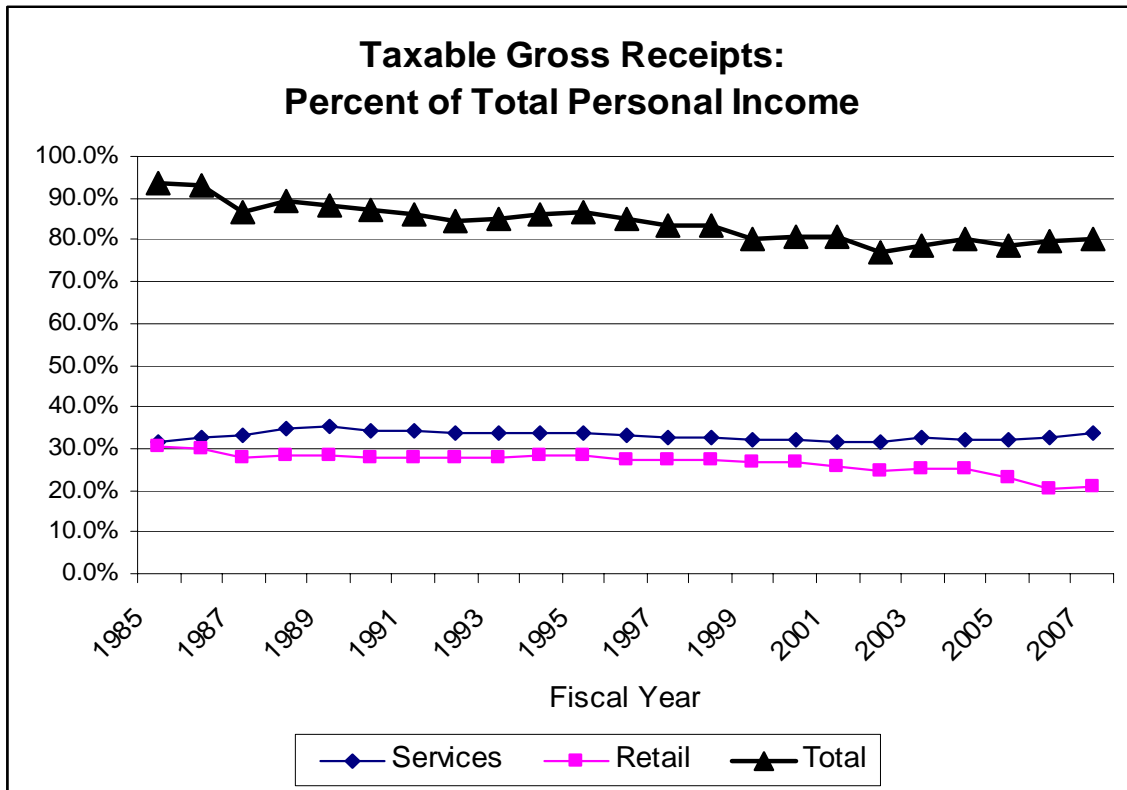
**Table 1**

<b>New Mexico Gross Receipts Tax Information by Major Industry</b>			
<b>Industry</b>	<b>FY 2007 Totals</b>		
	<b>Number of Returns</b>	<b>Taxable Gross Receipts</b>	<b>Gross Receipts Tax</b>
Agriculture, Forestry, Fishing and Hunting	5,073	81,905,240	5,429,889
Mining and Oil and Gas Extraction	9,222	2,088,617,224	128,139,588
Utilities	9,818	2,174,856,434	138,892,763
Construction	138,381	7,348,468,231	489,172,391
Manufacturing	46,314	1,375,358,313	86,968,280
Wholesale Trade	70,258	2,666,528,166	170,339,597
Retail Trade	242,754	12,407,109,985	849,006,651
Transportation and Warehousing	15,136	546,061,219	34,556,042
Information and Cultural Industries	55,743	1,099,371,411	71,878,009
Finance and Insurance	12,679	314,106,826	21,678,565
Real Estate and Rental and Leasing	40,115	805,920,956	54,357,255
Professional, Scientific and Technical Services	114,340	4,188,990,303	269,721,963
Management of Companies and Enterprises	1,337	49,042,584	3,492,335
Admin and Support, Waste Management	16,820	1,436,783,939	98,443,401
Educational Services	7,729	189,134,419	12,493,576
Health Care and Social Assistance	66,972	1,756,926,628	122,356,856
Arts, Entertainment and Recreation	8,097	148,072,263	9,874,456
Accommodation and Food Services	50,886	3,058,310,743	215,218,224
Other Services (except Public Admin)	260,809	6,032,493,417	395,260,894
Public Administration	2,004	489,523,325	27,309,169
Unclassified Establishments	6,239	55,712,231	3,624,101
<b>Total</b>	<b>1,180,726</b>	<b>48,313,293,857</b>	<b>3,208,214,007</b>

## GRT Growth Over Time

Figure 3 presents a history of the ratio of the GRT tax base, Taxable Gross Receipts or “TGR”, relative to Personal Income (“PI”). TGR has declined from about 90% of PI in the mid-1980’s to about 80% during the last several years. A significant portion of the decline is due to the Retail sector, which has fallen from 30% to 20%. The steep drop in that sector during the last two fiscal years is due to the deduction for food for home consumption, which took effect in the middle of FY 2005. TGR from Services have remained fairly constant at about one-third of PI.

Figure 3



Source: GRT and TGR from N.M. Taxation and Revenue Department, RP-80 Analysis of Gross Receipts Tax by Industry. Personal Income from FOR-UNM Economic Forecasting Service, Bureau of Business and Economic Research, University of New Mexico.

## **Pyramiding and the GRT on Services**

The GRT provides only limited exclusions from tax for transactions between businesses. Sales or leases of tangible property or licenses sold for re-sale or for leasing are deductible, as is tangible property used as a component or ingredient by manufacturers or construction contractors. Sales of a service for re-sale are deductible, but non-manufacturing and non-construction services are deductible if the service is considered “resold” and only if the re-sale of the service is itself subject to tax (i.e. in series of transactions, every other transaction would be taxable). In addition, several industry-specific deductions for sales of services have been introduced in recent years including software development services, aircraft maintenance, certain commissions, administrative and accounting services sold to an affiliate, etc.

In a study published in 2006, the N.M. Tax Research Institute calculated estimates of the amount of GRT that is collected from business-to-business transactions. The estimate was approximately 1/3 of total GRT. In FY 2007, that amount would be close to \$1 billion. Using similar information as was used to derive that estimate -- from the IMPLAN input-output tables and GRT data from the State -- we estimate that slightly more than half of the pyramided GRT is attributable to business-to-business sales of services. This result suggests that \$520 million of the total \$1.38 billion collected from service industries -- or about 38% -- is attributable to business-to-business transactions.

## **Treatment of Imported Exported Services, and New Mexico’s “use” tax**

Services performed in a New Mexico, as well as those performed outside New Mexico but delivered and initially used in New Mexico are included in the definition of *gross receipts*, however an exemption is provided for receipts from services performed outside the state, the product of which is initially used inside New Mexico. That exemption does not apply to research and development services however. Accordingly, the GRT’s companion *compensating* (“use”) *tax* is not imposed on imported services. In fact, the compensating tax applies to services almost only in the relatively rare circumstance of a service being acquired tax free for purposes of resale, but then not being resold in the subsequently taxable manner required by the statutory deduction. Another deduction is provided for gross receipts derived from services performed within New Mexico and sold to an out-of-state buyer. If the out-of-state buyer takes delivery or makes initial use of the product of the service in New Mexico, the deduction does not apply. Services performed both within and outside New Mexico are taxable only to the extent performed in New Mexico. “Reasonable” apportionment methods (i.e. direct labor hours) may be used for purposes of determining the New Mexico portion of multi-state services.

## **Other Policy Issues - Sourcing**

New Mexico's takes a "modified" origin sourcing approach to the taxation of goods and services, attributing tax to the "place of business" or office location of the seller for purposes of rate determination and local government tax distribution. Exceptions to this rule, where a destination approach is used, include construction sites, utilities, and real estate commissions. Home offices of resident sales personnel or other employees such as service technicians and office space provided by clients or customers under certain circumstances can create a "place of business" for purposes of gross receipts tax reporting. Services performed by those without a business location in the state report and the out of state rate (5%), which does not include county or municipal tax increments. Taxpayers with multiple places of business are allowed to report based on their method of crediting sales to the various locations, assuming the methodology is consistent and no obvious distortion results.