



***Tax Increase Discussions
New Mexico's Recent Dialogue,
Likelihood, and Expected Tax Proposals***

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NMTRI Principles of Good Tax Policy

N.M. Tax Research Institute is a non-profit, non-partisan member-supported organization dedicated to advancing the following principles of good tax policy in New Mexico:

- ***Adequacy***
 - Revenues should be sufficient to fund needed services
- ***Efficiency***
 - Interference with the private economy should be minimized
- ***Equity***
 - Taxpayers should be treated fairly
- ***Simplicity***
 - Laws, regulations, forms and procedures should be as simple as possible
- ***Comprehensiveness***
 - All taxes should be considered when evaluating the system
- ***Accountability***
 - Exceptions should be rare and should be carefully evaluated and justified

Economic Environment

- You heard David Abbey's excellent presentation:
 - REVENUE FORECAST - NOT PRETTY
 - Shortfall could still get worse
 - Further uncertainty around federal stimulus funds

Political Environment

- Broadening discussion of budget cuts and tax increases
- Social advocacy groups, religious groups and unions calling for more business and income taxes, less budget cuts
- Business advocacy and others calling for greater focus on gov't spending and no tax increases targeting business

Political Environment

- Most agree cuts are necessary
- Many concede tax increases may be inevitable
- Debate: If taxes are to be raised, which taxes and how much?
- Complication: Don't know how much tax revenue may be needed.

Tax Policy Issues

- Taxes are necessary in that they pay for public services, but:
 - Taxes can cause economic distortions, inefficiencies, and sometimes inequities
 - Economic implications of different tax increase proposals vary
 - The state needs to minimize negative impact of increased taxes on job creation as well as impacts on the most vulnerable

Executive Response

- Governor's "Balanced Budget Task Force:
 - 42 member representing general and special interests to discuss pros and cons of various tax increase options
 - Chair - Tax & Rev Secretary Rick Homans
 - NMTRD provided options and analysis
 - Useful effort in anticipation of upcoming session
 - Approach led to "man on the street" reactions in addition to special interest advocacy

Executive Response –Cont'd

- Balanced Budget Task Force Charge:
 - Not to vote on options or make recommendations
 - Keep in mind state competitiveness, improving the state's overall system, and be consistent with good tax policy principles
 - Reviewed list of varying and predictable tax options as compiled by the NMTRD

Legislature's Response

- Interim Committee Hearings Agendas Expanded:
 - Included tax increase options
 - Attempted focus on policy with expert panels
 - Coordinated with governor's task force
 - Differed in part with incentive restriction options not discussed by task force

Recent Developments

- Legislative Finance Committee:
 - Proposes reduced state budget but leaves \$200 million in unfunded appropriations
- Executive:
 - Proposes reduced budget with \$200 million shortfall
 - Suggest working with legislature to find \$200 million in “temporary” tax increases to make up difference

How Do New Mexico's Business Taxes Compare?

| Tax | New Mexico | U.S. Average | NM – U.S. Aver. |
|--------------------------------|-------------------|---------------------|------------------------|
| | (% of GSP) | (% of GSP) | Annual Revenue |
| Property Tax | 0.8% | 1.7% | (\$600 million) |
| Sales Tax on Inputs | 1.9% | 1.1% | \$520 million |
| Excise | 0.5% | 0.6% | (\$60 million) |
| Corp. Income Tax | 0.5% | 0.5% | -- |
| UI Tax | 0.2% | 0.3% | (\$70 million) |
| Ind. Income Tax on Bus. Income | 0.1% | 0.2% | (\$45 million) |
| Other | 2.1% | 0.5% | \$955 million |
| Total | 6.0% | 4.9% | \$700 million |

Source: "Total state and local business taxes," Ernst & Young, Council on State Taxation, January 2009.

Tax Proposals

- Include most significant tax programs
- Are often “retreads” of previous proposals
- Don’t represent the only options
 - Endless options/“variations on a theme” possible
- Some options from blue ribbon tax reform commission
- Include compliance enhancement proposals that don’t “raise taxes”

General Fund Revenue Impacts of Various Revenue Raising Options

(Dollar amounts in millions)

| Income tax options: | Effect Date | FY10 | FY11 | FY12 |
|--|--------------------|-------------|-------------|-------------|
| 1% income tax increase on current top bracket (married \$24,000/single \$16,000) | Tyba 1/1/2010 | 25.5 | 170.0 | 179.4 |
| 1% income tax increase over \$100,000 (single), \$150,000 (married) | Tyba 1/1/2010 | 5.0 | 56.1 | 59.4 |
| Addback income tax deduction for state & local taxes | Tyba 1/1/2010 | - | 40.0 | 42.0 |
| Reduce deduction for capital gains from 50% to 25% | Tyba 1/1/2010 | - | 18.0 | 20.0 |

| Corporate income tax options: | | | | |
|--|---------------|---|------|------|
| Require combined reporting for corporate income tax | Tyba 1/1/2011 | - | 12.0 | 30.0 |
| Increase corporate franchise tax from \$50 to \$250 per year | Tyba 1/1/2010 | - | 7.5 | 7.5 |

| Gross receipts tax options: | | | | |
|--|----------|---|-------|-------|
| Repeal GRT deduction for food | 7/1/2010 | - | 228.0 | 238.9 |
| Repeal GRT food deduction and reinstate 0.5% GRT credit in muni areas | 7/1/2010 | - | 48.0 | 48.0 |
| Repeal GRT deduction for medical services | 7/1/2010 | - | 65.0 | 69.9 |
| Apply compensating tax to in-state sales currently exempt from all tax | 7/1/2010 | - | 13.2 | 13.8 |
| Increase statewide GRT rate by 0.25% | 7/1/2010 | - | 126.0 | 132.0 |

| Excise tax options: | | | | |
|---|----------|------|------|------|
| Increase motor vehicle excise tax by 1.0% | 4/1/2010 | 7.7 | 34.3 | 37.7 |
| Increase O&G Emergency School Tax on oil by 1% | 4/1/2010 | 10.1 | 40.4 | 41.8 |
| Increase O&G Emergency School Tax on gas by 1% | 4/1/2010 | 10.8 | 52.8 | 53.8 |
| Increase liquor excise tax by 5 cents per drink | 4/1/2010 | 10.0 | 40.0 | 40.7 |
| Increase insurance premiums tax on health insurance by 1% | 1/1/2011 | - | 22.0 | 47.0 |
| Increase cigarette tax by \$1 per pack from \$0.91 to \$1.91 per pack | 4/1/2010 | 7.5 | 30.0 | 30.0 |
| Increase cigarette tax by \$1 with no exemption for tribal sellers for increase | 4/1/2010 | 24.8 | 99.0 | 99.0 |
| Increase tobacco products tax from 25% to 40% | 4/1/2010 | 0.8 | 3.0 | 3.0 |

| Options to reduce tax expenditures: | | | | |
|---|---------------|-----|------|------|
| Repeal angel investor tax credit | Tyba 1/1/2010 | - | 0.8 | 0.8 |
| Reduce film production credit rate from 25% to 15% of expenditures | Tyba 1/1/2010 | 6.5 | 26.0 | 28.6 |
| Reduce rate of high wage jobs tax credit from 10% to 7% of wages | 7/1/2010 | - | 5.0 | 5.5 |
| Reduce rate of technology jobs tax credit from 8% to 6% of expenditures | 7/1/2010 | - | 1.5 | 1.7 |
| Reduce rate of investment credit from 5% to 4% of expenditures | 7/1/2010 | - | 1.6 | 1.8 |
| Reduce renewable energy production credit by 20% | Tyba 1/1/2010 | - | 1.0 | 1.1 |
| Freeze hospital GRT credit at FY10 level | 7/1/2010 | - | 4.0 | 8.0 |
| Reduce rate of credit for NMMIP assessments by 20% | 7/1/2010 | - | 10.0 | 14.0 |
| Eliminate GRT back to school tax holiday | 7/1/2010 | - | 2.7 | 2.7 |
| Reduce lab small business partnership credit by 50% | 7/1/2010 | - | 2.0 | 2.1 |

"Tyba" = Tax years beginning on or after.

Source: Legislative Finance Committee

Tax Proposals-Personal Income Tax

- “Roll Back Richardson Tax Cuts”
- Tax rate “surcharge” at varying income levels
 - NM rates similar to surrounding states currently
- Reduce capital gain tax preference
 - NM more generous than most states
- Add-back state tax deduction to NM taxable income
 - Majority of states and neighbors require add-back

Tax Proposals - Corporate Income Tax

- Impose mandatory combine reporting
 - NM currently imposes highest rates and least favorable reporting rules relative to surrounding states but for filing group elections
- Impose higher franchise tax (currently \$50/yr)
- Franchise tax based on apportionment factors

Tax Proposals - Gross Receipts Tax

- Increase rates
 - Compensating tax implications
- Eliminate or alter “hold harmless” provisions
- Repeal or alter “food tax” deduction
 - Candy & soda
- Other

Other Taxes

- Oil and gas taxes
 - “Equalize” oil and gas tax rates
 - Progressive rate structure
- Impose higher “sin” taxes
 - Alcohol
 - Cigarettes
 - Tribal exemption issue
- Increase gasoline taxes
 - Tax currently goes to road fund

Other Taxes

- Motor vehicle excise tax
 - NM low at 3% with little ED implication
 - Turnover taxes so rate should be less than GRT
 - Sector still in downturn.
- Insurance premiums tax
 - Increase health premiums 1% - why health
 - Many health services now out of GRT base
 - Retaliatory taxes

Business Incentives

- Governor's Task Force
 - Adopt uniform language and requirements, performance standards, recapture, etc.
 - Require additional reporting, evaluation
- Legislative Options
 - Reduce credit percentages (i.e. film credit from 25% to 15%, HWJTC from 10% to 7% of wages)

Note: Film Credit more costly than all business incentives combined

Other Taxes

- Uranium and Coal Taxes
 - Repeal coal surtax exemption
 - Not general fund revenue source
 - Increase uranium tax
 - No uranium mining currently taking place in NM
- Estate Taxes
 - De-couple from federal credit

Non-Tax Revenue Enhancement Proposals

- Pass-through entity (“PTE”) and oil and gas proceeds withholding
- Tax remittance on government purchases by governmental entities
- Require in-state contractors to post bonds
- Increases penalties and reallocation authority
- Reduce O&G severance taxes with commensurate increase in emergency school tax rate

Summary

- Revenue/budget situation uncertain but bleak
- Taxes increase proposals WILL be introduced
- Taxes increases of some sort are probable
- Tax remittance on government purchases by governmental entities
- How you tax matters – do the least harm