



***Tax System Overview and  
Budget and Tax Policy Actions  
of the 2009 Legislative Session***

**May 13, 2009**

**Richard Anklam, Executive Director**

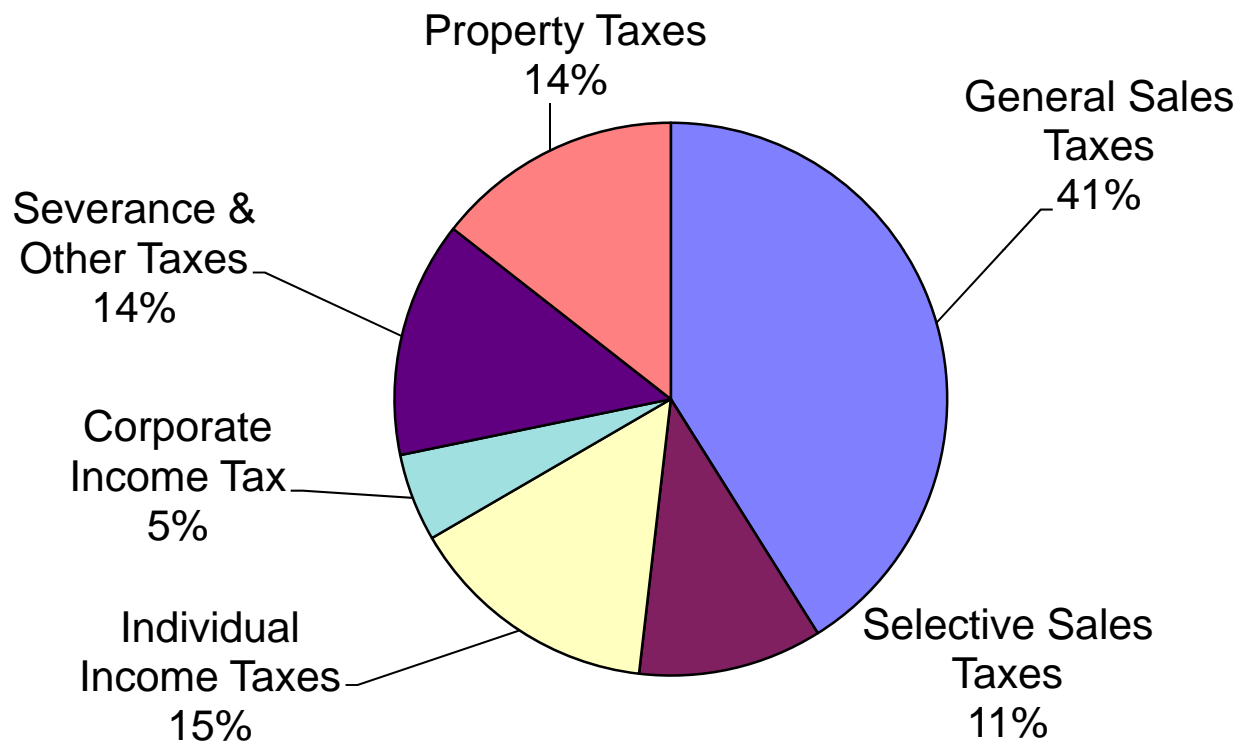
**Thomas Clifford, PhD, Research Director**

## ***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:*

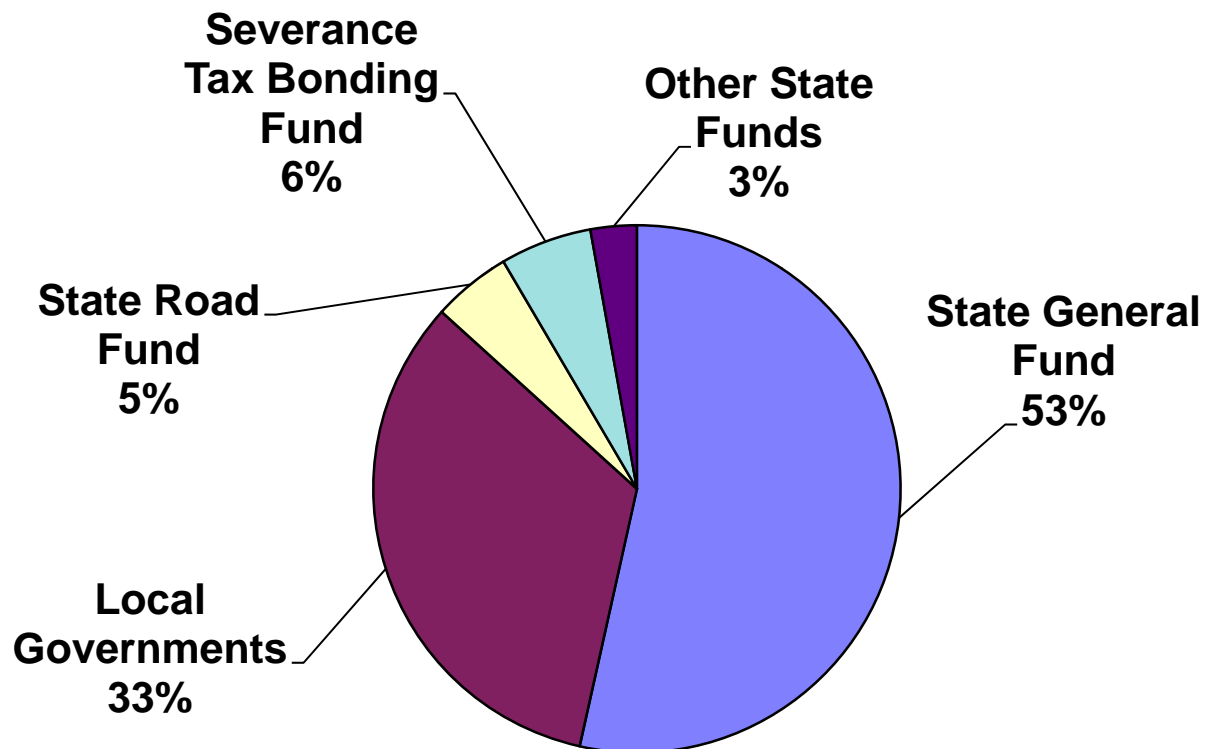
- **Adequacy**
  - Revenues should be sufficient to fund needed services
- **Efficiency**
  - Interference with the private economy should be minimized
- **Equity**
  - Taxpayers should be treated fairly
- **Simplicity**
  - Laws, regulations, forms and procedures should be as simple as possible
- **Comprehensiveness**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

## ***FY 2007 State & Local Tax Collections: \$7.9 Billion***



- High reliance on general sales taxes
- Low reliance on property taxes
- High reliance on severance taxes
- About half of selective sales taxes are road fund revenues.

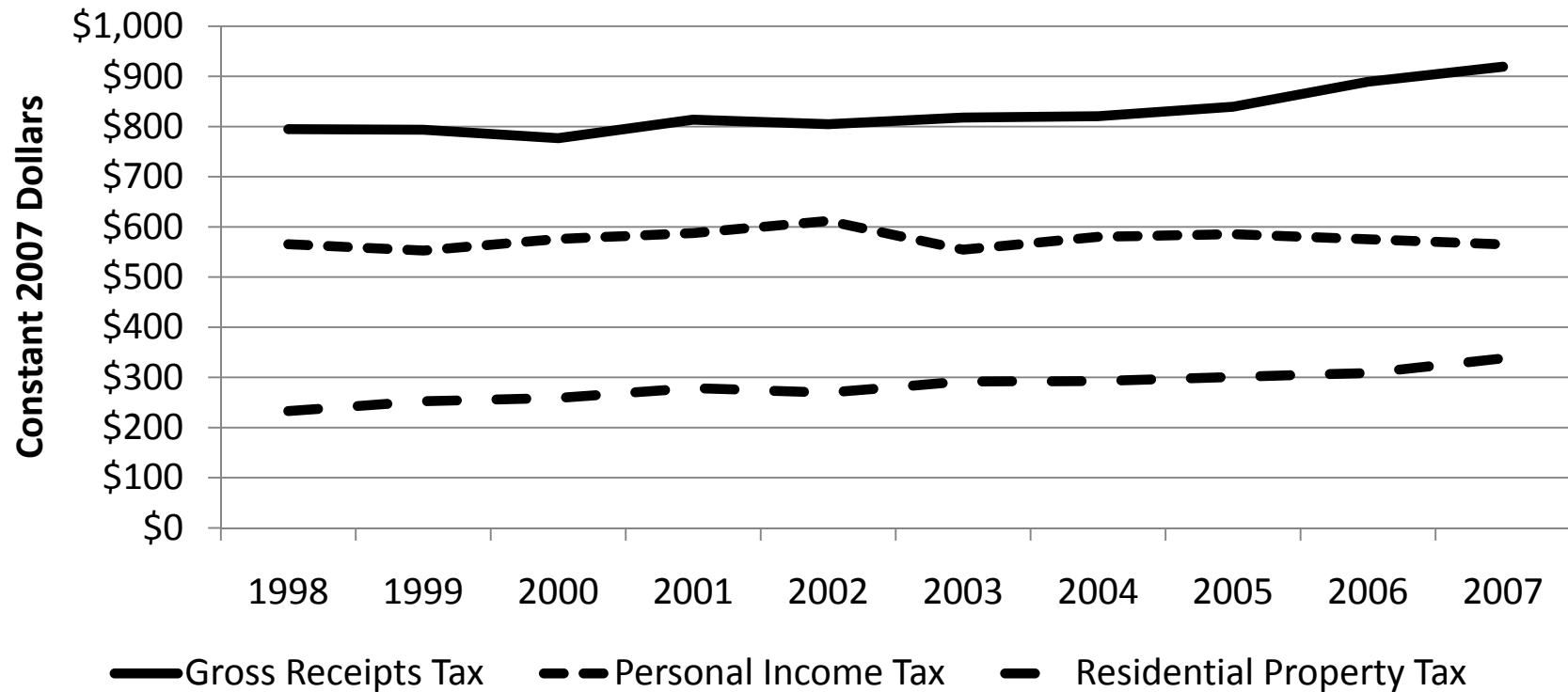
## ***FY 2007 Tax Revenue Distributions: \$7.9 Billion***



- Just over half of all tax revenue goes to the state's General Fund
- Local governments receive about one-third of all tax collections.

## *Trends in Broad-based Tax Collections*

### Annual Real Per Capita Tax Collections



- GRT has increased – construction, O&G, Lab spending plus rate changes
- Property tax has increased due to assessed value growth
- Income tax collections flat due to tax rate reductions.

## *Multistate Comparisons: FY 2002*

	<i>Measure:</i>	<i>Rank:</i>	<i>NM as Percent of U.S. Average:</i>
1	State & local general revenue -- % of personal income	3rd	128%
2	State & local taxes as percent of personal income	9 <sup>th</sup>	107%
3	Property taxes as a percent of personal income	46 <sup>th</sup>	54%
4	Sales taxes as a percent of personal income	6 <sup>th</sup>	142%
5	Income taxes as a percent of personal income	36 <sup>th</sup>	82%
6	Motor fuels taxes as a percent of personal income	22nd	121%
7	Motor vehicle excise tax rate	37th	61%
8	Cigarette tax rate	20th	105%
9	State & local taxes on high-income families (2004)	30th	100%
10	State & local taxes in the largest city (2004)	31st	93%
11	State & local business taxes as a percent of gross state product*	11th	120%

Source: Congressional Quarterly, State Fact Finder. Except \*COST, Annual Business Tax Study excluding severance taxes.

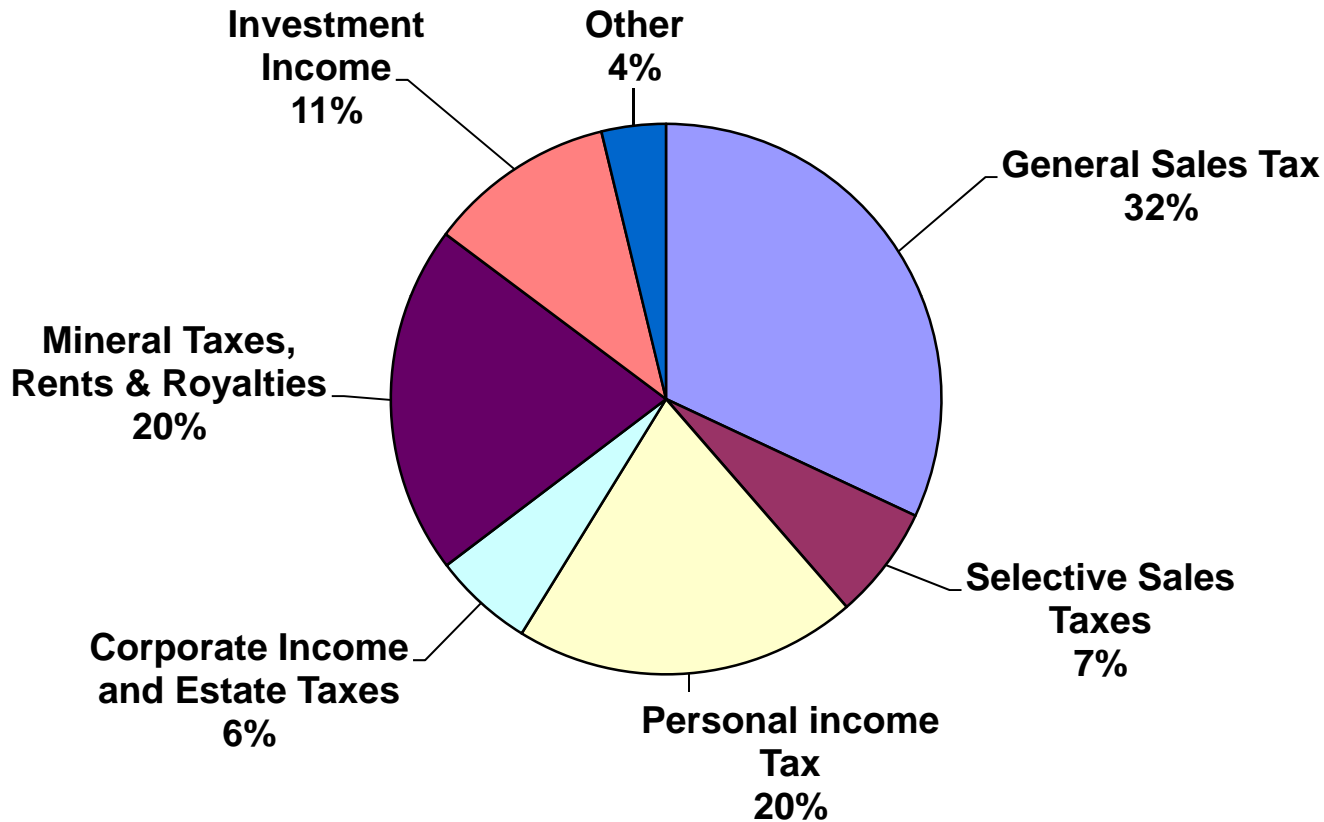
- New Mexico's state & local sector uses a relatively large proportion of total personal income.
- N.M. relies heavily on sales tax, lightly on property tax and below average on Income tax.
- Taxes imposed directly on businesses – rather than on households – are relatively high.

## *How Do New Mexico's Business Taxes Compare?*

<b>Tax</b>	<b>New Mexico</b>	<b>U.S. Average</b>	<b>NM – U.S. Aver.</b>
	(% 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
<b>Total</b>	<b>6.0%</b>	<b>4.9%</b>	<b>\$700 million</b>

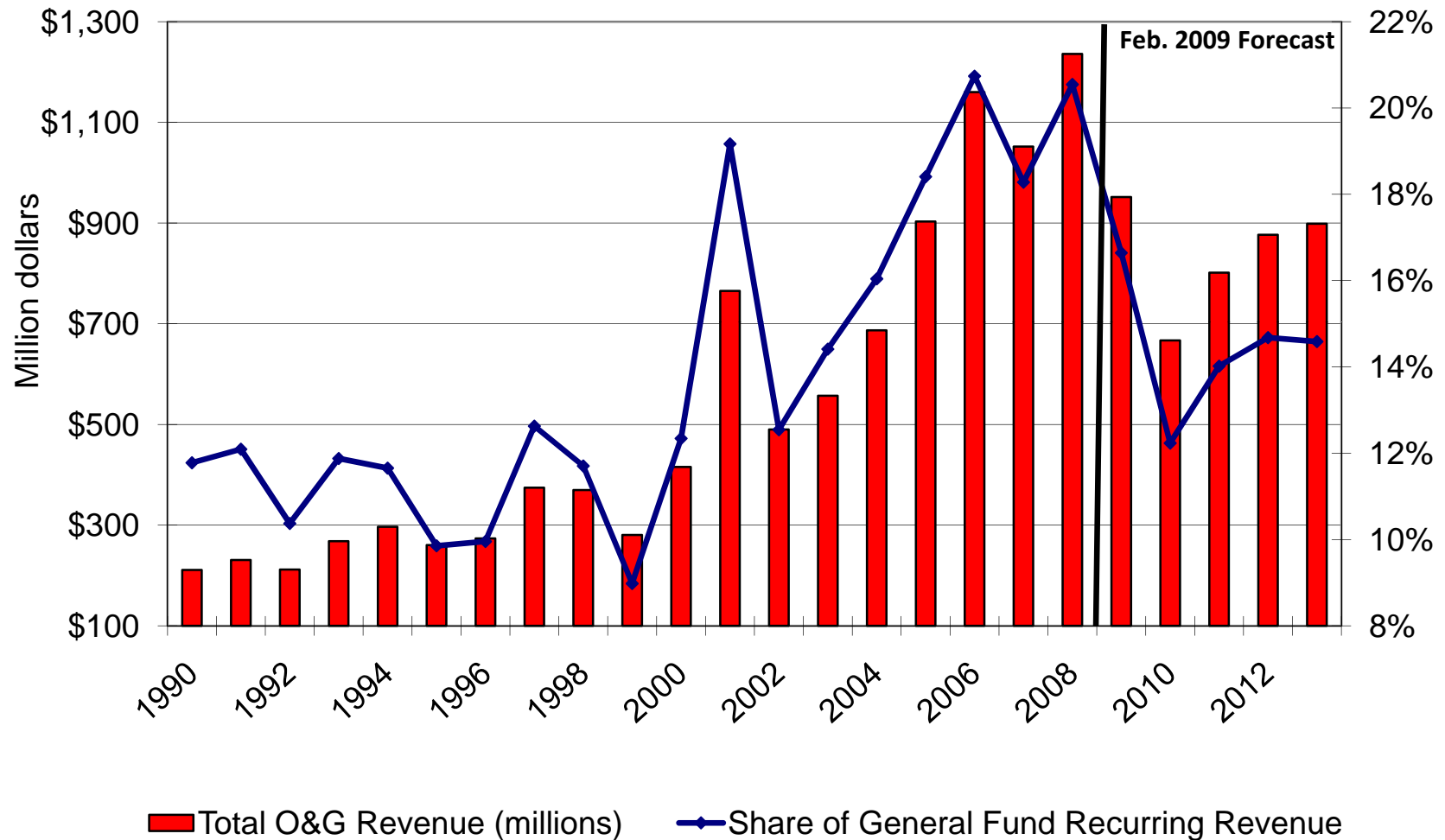
Source: “*Total state and local business taxes,*” Ernst & Young, Council on State Taxation, January 2009

*General Fund “Own-Source” Revenue:  
FY 2008 Total \$6.0 Billion*



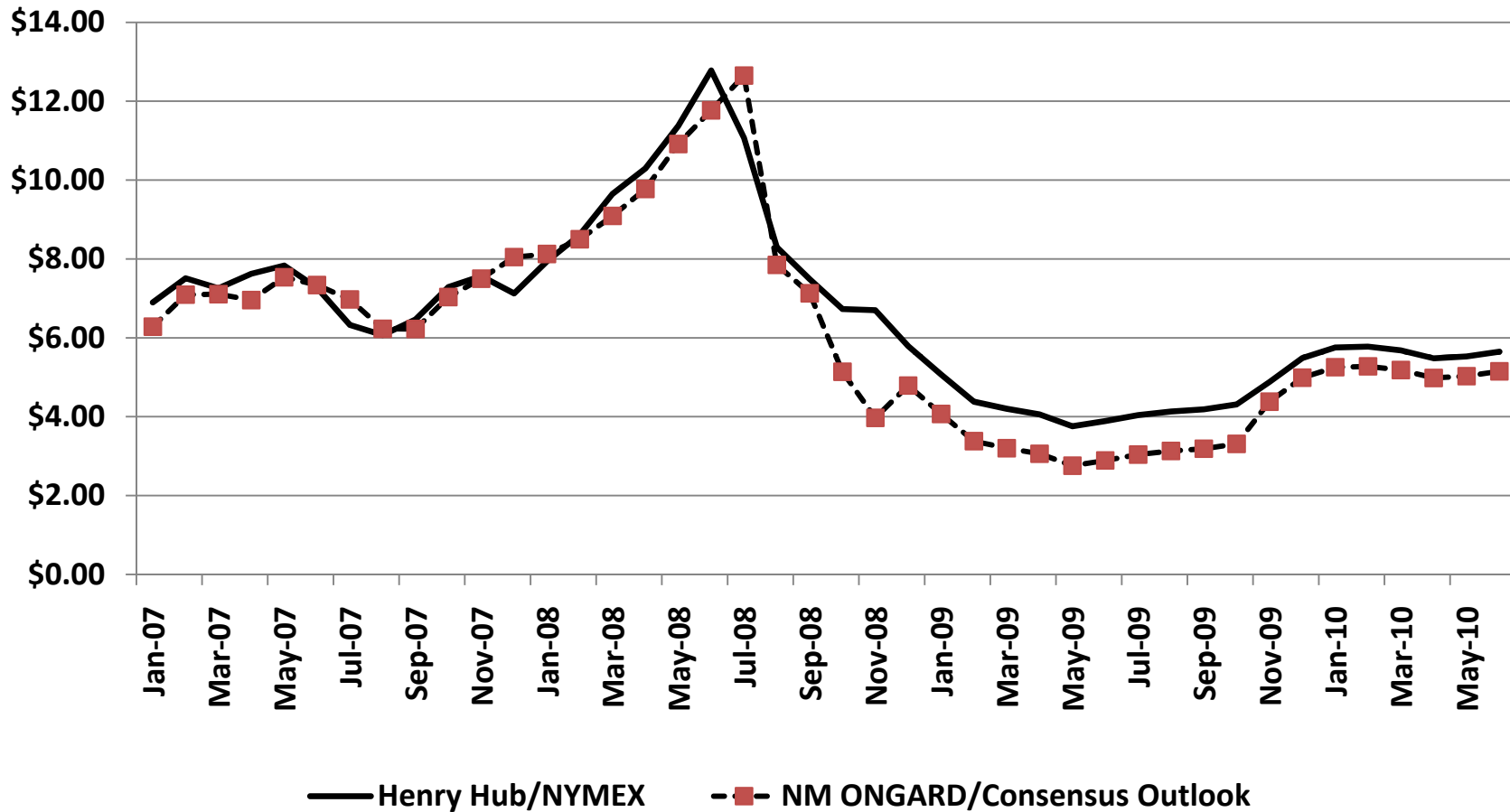
- State revenues are well balanced, though O&G share at historic highs
- About 1/3 from non-tax revenues – O&G and Permanent Fund earnings

## General Fund Revenue from Oil and Gas Taxes, Rents and Royalties



*Oil & gas revenues cause major fluctuations in total General Fund revenue*

## Natural Gas Price History and Forecast

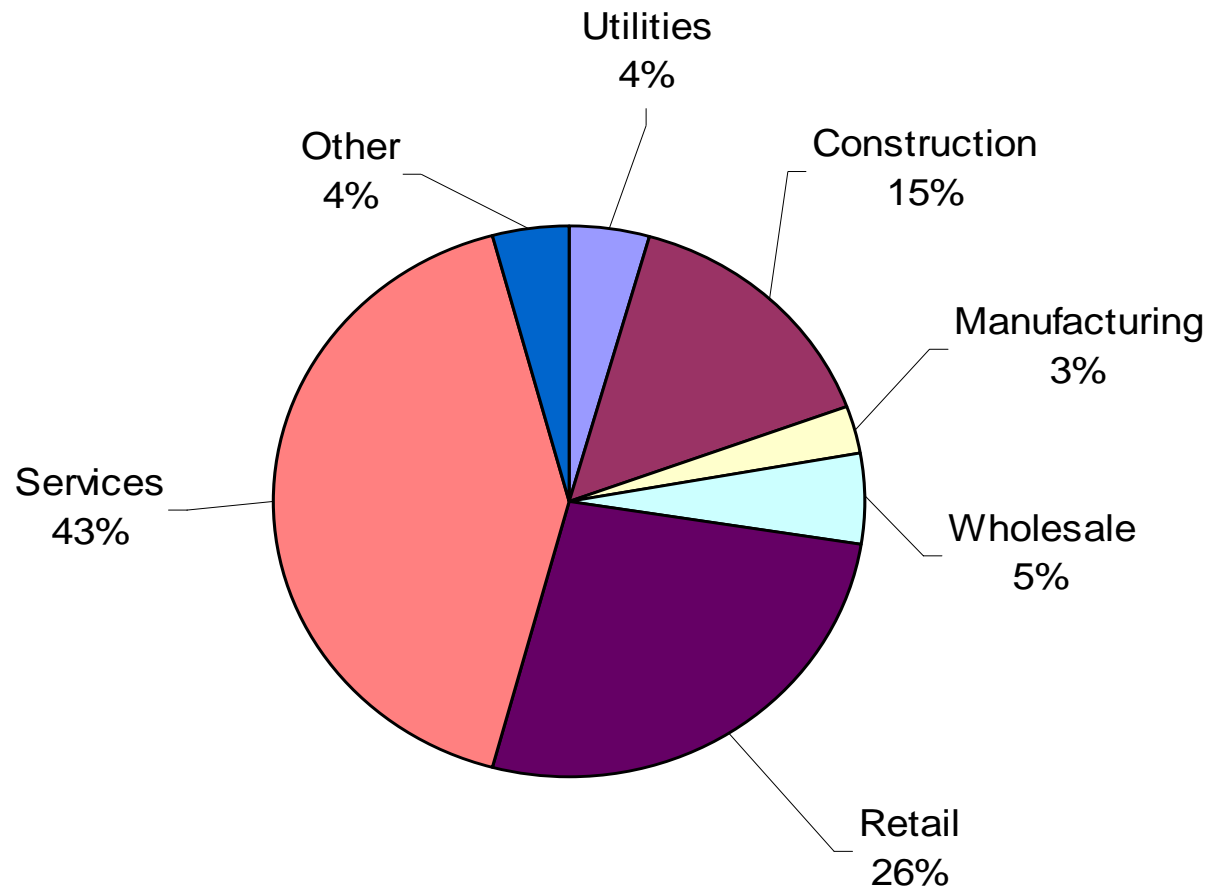


*Gas prices are expected to increase significantly over the coming year.*

*NM price usually tracks Henry Hub, but differences can be large at times.*

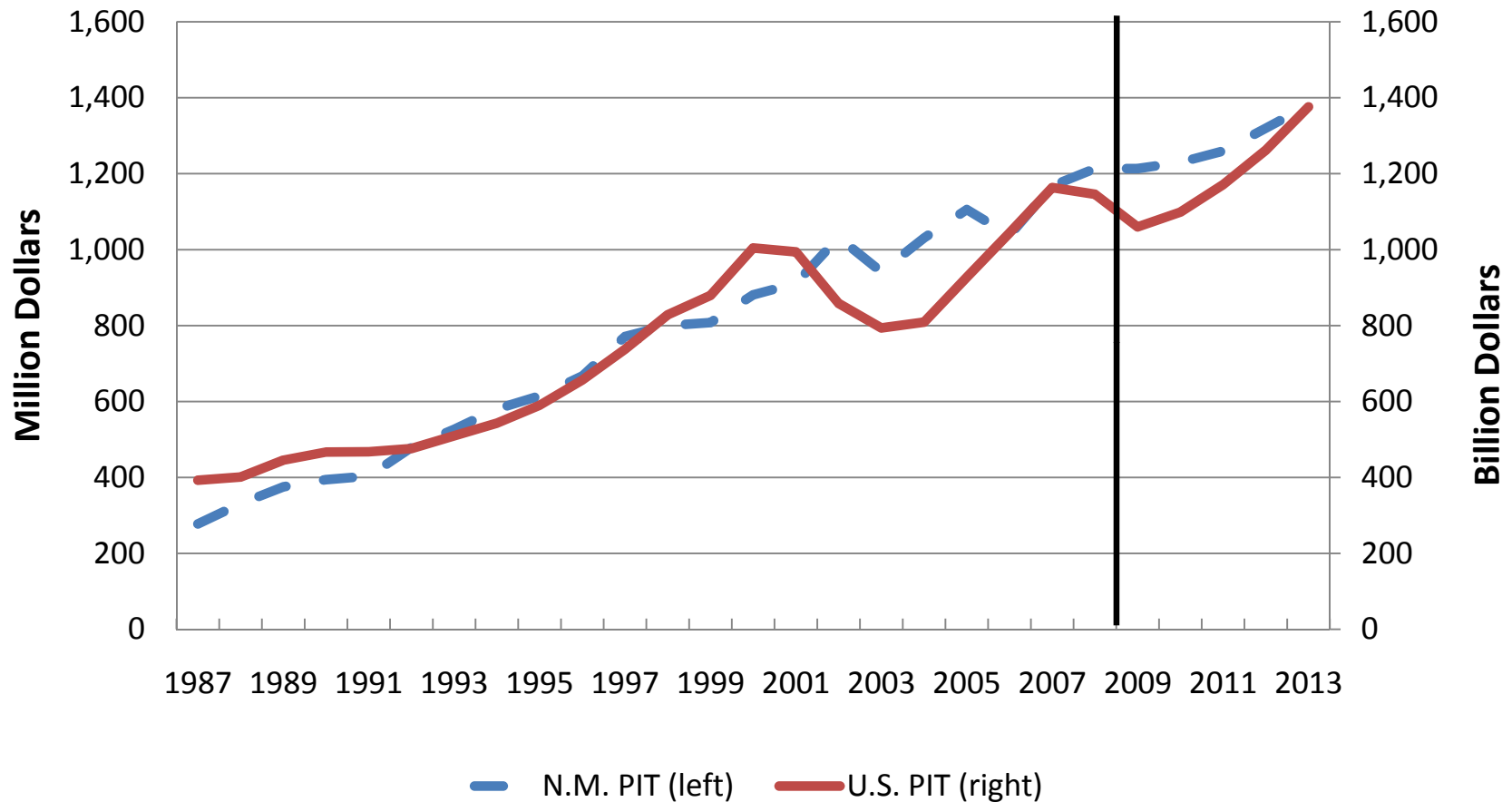
*General Fund revenue **decreases \$10 million for every 10-cent change in annual price***

## New Mexico Gross Receipts Tax by Industry Group: FY 2007



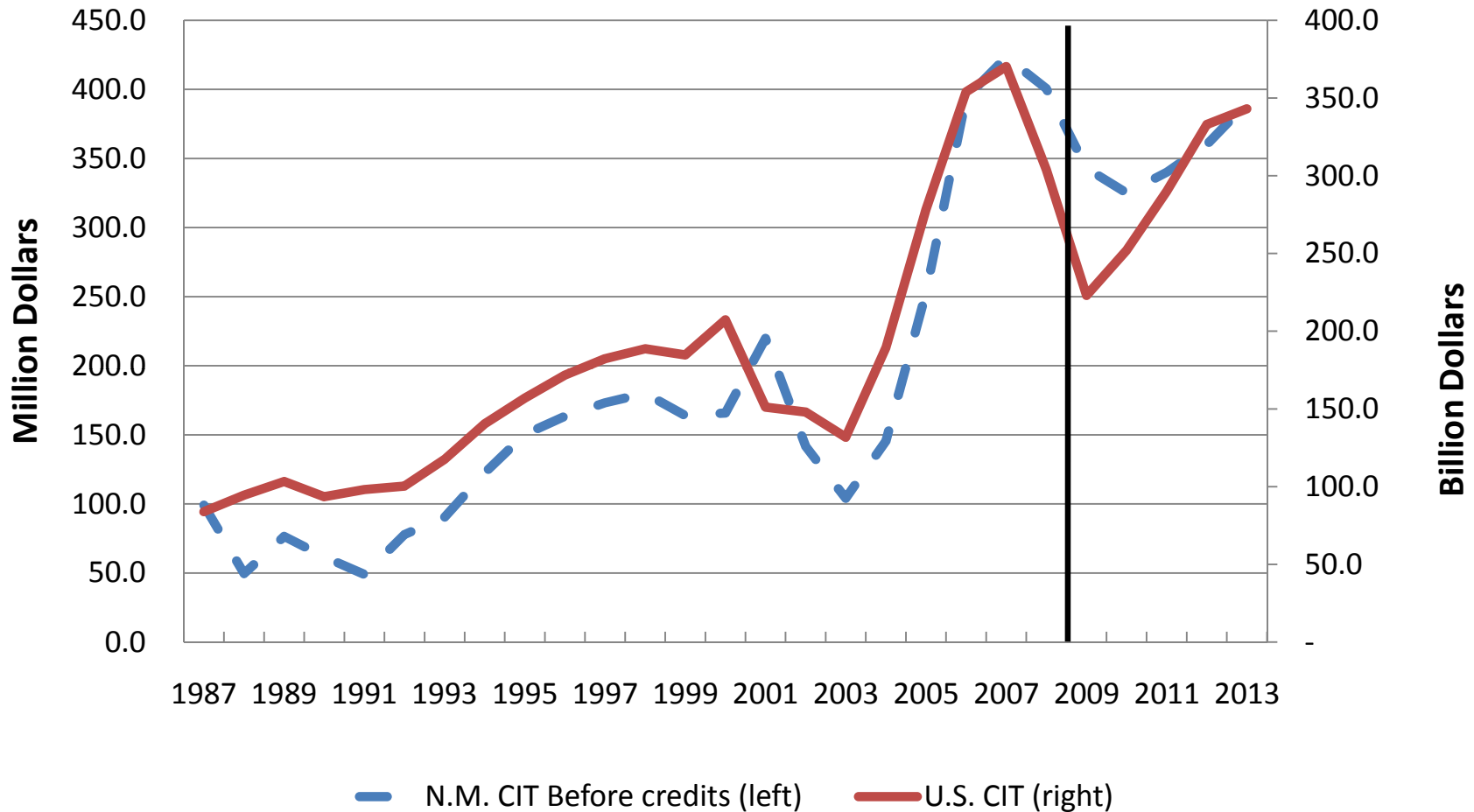
- GRT = “New Mexico’s Services Tax”
- Comprehensive tax base makes GRT less sensitive to recession
- Estimated 1/3 of tax base derived from business-to-business transactions

## NM vs US Individual Income Tax Collections



- *New Mexico is forecasting a milder downturn than the U.S.*
- *Federal decline in 2002 – 2005 partly due to law changes*
- *NM growth from 2004 – 2009 slowed by rate changes.*

## NM vs US Corporate Income Tax Collections



- *Federal forecast steeper decline, steeper recovery*
- *NM NOL treatment should postpone, prolong decline*
- *Film credits reduce NM collections by \$50 million per year*

## *2009-2010 Budget Actions Overview*

- Forecast 2009 revenue fell by 12% between July 2008 and February 2009
- 2009 revenue fell almost \$500 million short of appropriations
- Solvency package adjusted 2009 appropriations and shifted balances to rebuild reserves to 10%
- 2010 budget relied on sharp increase in federal funding to maintain flat spending

## February 2009 General Fund Consensus Forecast

	2009		2010	
	(\$ million)	Change from Prior Year	(\$ million)	Change from Prior Year
Gross receipts & Comp	1,973	2.6%	1,980	0.4%
Selective sales taxes	405	1.2%	419	3.4%
Income tax	1,214	0.0%	1,230	1.4%
Corporate income tax	293	-17.4%	275	-6.1%
Oil and gas taxes	411	-34.3%	335	-18.6%
Investment Income	685	3.5%	676	-1.2%
Oil & gas royalty	541	-11.4%	332	-38.5%
Other	198	-12.4%	204	2.8%
<b>Total</b>	<b>5,719</b>	<b>-4.9%</b>	<b>5,451</b>	<b>-4.7%</b>

FY 2009 Income tax amount is not reduced for 2008 rebates of \$55.7 million.

- FY 2010 assumptions: oil \$47 per barrel, natural gas \$4.80 per thousand cubic feet. Prices expected to increase in subsequent years.
- Individual income tax and gross receipts tax collections are not expected to decrease during the 2009-2010

**General Fund Financial Summary -- February 2009 Update**  
**(Million dollars)**

	<u>2008</u>	<u>2009</u>	<u>2010</u>
Beginning Balance	651	714	218
<b>Revenue:</b>			
Recurring revenue	5,995	5,703	5,451
Nonrecurring revenue	47	(56)	-
<u>Other</u>	<u>50</u>	<u>17</u>	<u>48</u>
Total	6,091	5,665	5,499
<b>Appropriations:</b>			
Recurring	5,675	6,027	5,201
Non-recurring	295	75	
Other	58	58	-
<u>Total</u>	<u>6,028</u>	<u>6,160</u>	<u>5,201</u>
<b>Net Change in Reserves</b>	<b>63</b>	<b>(495)</b>	<b>298</b>
Ending Reserves	714	218	516
Ending balance as % of appropriations	12%	4%	10%

- Before legislative action, balances fell to 4%, 2010 appropriations would have to be 14% below 2009 to restore a 10% reserve.

## ***Solvency Package***

In four separate bills the Legislature addressed the estimated \$450 million shortfall in FY 2009:

- HB 9 cancelled General Fund capital outlay projects (some replaced with Severance Bond Finding): \$91.6 million one-time savings
- HB 10 reduced appropriations in FY 2009 by \$163 million recurring savings
- SB 79 swept unused balances into the General Fund: \$130 million one-time re-allocation.
  - \$64 million from public school capital outlay. The LFC hopes that federal stimulus money would more than offset this reduction.
- SB 80 mandated a first quarterly estimated payment of corporate income taxes: \$65 million (one-time acceleration).

## *2010 Budget Approved by the Legislature*

- Total spending **from all sources** increases by 1.5% or \$215 million to a total of **\$15.0 billion**
- State General Fund spending decreases by \$519 million or 8.6% to \$5.5 billion;
  - Spending is approximately equal to forecast General Fund revenue
- Federal spending increases by \$646 million or 13%
- Other State funds increase by \$163 million or 6%
- Public School Support decreases by \$37 million or 1.2%
- Health spending increases by \$239 million or 4.4%

## ***Tax Legislation Approved***

- Restored first quarter estimated payment of CIT (Ch. 4, SB 80)
- Manufacturing incentives extended from 2011 to 2020 (HB 75):
  - More generous Investment Credit rules
  - Double-weighted Sales apportionment election
- Renewable energy subsidies:
  - New PIT/CIT tax credits for renewable power plant investments (Ch. 279, SB 237)
    - Non-proportional allocation of credits among owners
  - Expanded PIT credits for solar (Ch. 243, SB 257)
  - Expanded sustainable buildings PIT/CIT credit (Ch. 59, SB 291)
    - Credits earned by non-profits transferable
  - New PIT/CIT credit for geothermal heat pumps (Ch. 271, HB 375)
  - Exemption for re-cycled biodiesel fuel (Ch. 99, HB 554)

## ***Tax Legislation Approved (cont.)***

- Local government issues:
  - Health care GRT options extended for Bernalillo (1/16%) (Ch. 61, HB 135) and San Juan, Sierra & Torrance Counties (Ch. 16, SB 89)
  - 0.5% Environmental GRT increase for Ruidoso and Ruidoso Downs (SB 324)
  - TIDD-financed bonds approved for Winrock Mall (Ch. 58, SB-467)
- New requirements for TIDD GRT intercepts (Ch. 179, HB-451)
  - Notification to State agencies
  - State representation on TIDD Boards
  - Revenue in excess of bond debt service reverts to earmarking government

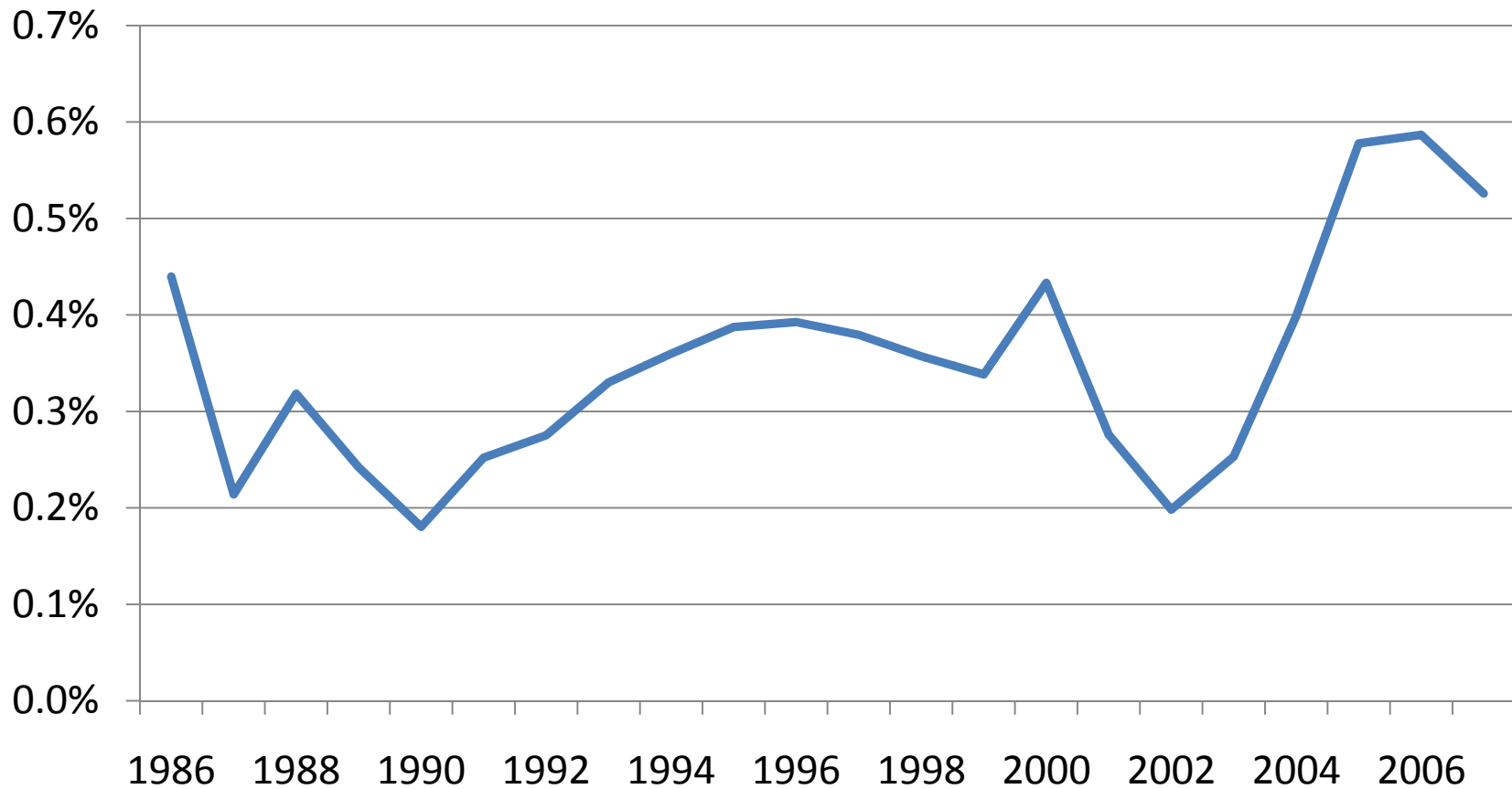
## ***Tax Legislation Approved (cont.)***

- Property tax issues:
  - Authorized special districts for financing solar panels (SB 647)
  - Require sellers to provide new residential buyers an estimate of likely property tax liability (Ch. 165, HB 261)
  - Exemption for mutual domestic water association property (Ch. 246, HB 297)
  - Solar energy special assessments (Ch. 270, HB-572)
  - Special valuation method for wastewater systems (Ch. 247, HB 388)
- Tax administration:
  - Re-write confidentiality provisions of the T.A.A. (Ch. 243, HB 257)
  - Cigarette tax act enforcement amendments (Ch. 197, SB 219)
  - New civil penalties for weight-distance tax non-compliance (Ch. 196, SB 213)

## ***Tax Legislation Not Approved***

- Tax increase for education (HB 346)
  - Initially 0.5% GRT + 1.1% PIT
  - House approved 0.75% GRT = \$400 million/year
  - Senate Corporations Committee DNP
  - Concerns over economy & uncertainty about future budgets
- Corporate income tax combined reporting mandate (SB 389):
  - Fiscal impact uncertainty – Treatment of NOL's?
  - Definition of “unitary” not clarified in the bill
  - Eliminates federal consolidated reporting option
  - “Joyce/Finnegan” not addressed
  - Effective immediately
  - Impacts on recently re-located firms?

## NM Corporate Income Tax Share of Gross State Product



- No evidence of chronic CIT base erosion due to aggressive tax planning.
- State-level CIT hard to justify from tax policy perspective

## ***Tax Legislation Not Approved***

- Franchise tax increase/Corporate income tax decrease (SB 648):
  - New “minimum tax” based on UDITPA payroll, property & sales
  - Reduced CIT rates, but \$80 million tax increase overall
  - Large “zero bracket” would reduce number of taxpayers, fewer taxpayers would pay more liability, increasing their tax burden
  - All 20%-owned entities included on return
  - S-corporations included
- Withholding tax requirement for pass-through entities (HB 8, 404):
  - Most PTE’s withhold quarterly on owner’s net income
  - Applies to in-state & out-of-state shareholders
  - Estimated \$20 million increase in collections through improved compliance

## ***Tax Legislation Not Approved (cont.)***

- Personal income tax re-write (HB 262):
  - Change current exemption/deductions/credits to a table of credits
  - Drop piggybacking on federal exemptions and deductions
  - Index new credits for inflation
- Property tax relief from “tax lightning” (HB 160, SB 181)
  - 3% value increase limit would continue when a house is sold
  - New houses would be valued like existing homes
  - Existing homes would have values “rolled back”
  - Yield control would increase tax rates in response to lower values creating a tax shift
  - Debt service capacity would decrease

## ***Tax Legislation Not Approved (cont.)***

- TIDD proposals:
  - Bonds for Suncal/Westland development (HB-470, SB-249)
  - Limits on TIDD's (HB-392, SB-483, SB-509, SB-576)
- Tax increases:
  - Personal income tax rate increase (HB 64)
  - Addback State income taxes deducted by itemizers (SB-523)
  - Motor vehicle excise tax (HB-649)
  - Cigarette tax (HB-742)
  - Greenhouse gas registry fees (HB-98)
  - Liquor tax (HB-57, HB-528)
  - Uranium resource excise tax (HB-84)

## ***Tax Legislation Not Approved (cont.)***

- TRD Administrative proposals:
  - Lower e-filing requirement threshold (HB-266)
  - TRD join IRS state tax levy program (HB-490)
  - TIDD formula re-write (SB-201)
- Miscellaneous new deductions/credits/exemptions
  - Small business R&D GRT credit extension (SB-45)
  - Health care GRT (HB-509, HB-510, HB-680)
  - Child care GRT (HB-359)
  - Military retirees PIT (HB-276)
  - Film industry GRT exemption (HB-404)
  - Military base construction GRT (HB-67)
  - Hybrid vehicle MVX exemption extension (HB-89)

## *Summary*

- Federal Stimulus funds postponed N.M.'s day of reckoning
  - If current revenue projections are accurate, the state will get through FY 2010 with modest budget cuts and no major tax increases
  - Future budget years may present challenges if oil and natural gas prices do not increase significantly
- Tight budgets left little room for tax cuts
- When packaged with education spending increases, a significant tax increase was approved by the House but rejected by the Senate.
- Tax policy was dominated by spending demands on one hand and concerns about the impacts of tax increases on the economy on the other.