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

ORIGINAL DATE 2/05/2016
SPONSOR Padilla **LAST UPDATED** **HB**

SHORT TITLE Broadband Telecom Facility Gross Receipts **SB** 247

ANALYST Alejandro

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY16	FY17	FY18	FY19	FY20		
$0.0	($1,100.0 - $24,000.0)	($1,100.0 - $24,100.0)	($1,200.0 - $24,200.0)	($1,400.0 - $24,400.0)	Recurring	General Fund

(Parenthesis ( ) Indicate Expenditure Decreases)

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY16	FY17	FY18	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
Total	$28.0			$28.0	Nonrecurring	TRD Budget

(Parenthesis ( ) Indicate Expenditure Decreases)

SOURCES OF INFORMATION
LFC Files

Responses Received From
Taxation and Revenue Department (TRD)

SUMMARY

Synopsis of Bill

Senate Bill 247 proposes enacting a new section of the Gross Receipts and Compensating Tax Act that would provide a deduction for broadband telecommunications network facilities from the gross receipts tax and compensating tax on components and construction services. To qualify, systems must have download speed of at least 10 megabits per second and upload speed of one megabit per second.

The bill's purpose is to promote the deployment of broadband telecommunications services in New Mexico.

The proposed effective date of this bill is July 1, 2016, and the sunset date is July 1, 2026.

FISCAL IMPLICATIONS

Under its Connect America Fund, designed to extend broadband network access to rural communities throughout the country, the Federal Communications Commission (FCC) recently awarded Century Link and Frontier a combined $15.4 million to expand their networks in New Mexico. The funding will recur annually for six years, and is intended to supplement the firms' capital investment and operating expenses to bring broadband service to approximately 25,000 residences and business that are not currently connected.

LFC staff estimated the minimum annual revenue impact of this bill at $1.1 million based on the $15.4 million in annual FCC funding. However, the revenue impact could be higher depending on the amount of capital that Century Link and Frontier invest in these projects as well as broadband network expansion projects that may be undertaken in the future.

The higher range figures in the table above were calculated by TRD and represent a more comprehensive estimate of the potential impact of the bill. TRD took into consideration a paper[1] published by the FCC that examined the composition of broadband network operating costs in both urban and rural areas. The paper highlights that capital expenses of broadband network communications are significant (see detailed discussion for more information) and recommends the leveraging of commercial technologies to achieve greater communications capabilities and to reduce costs. Also, because broadband telecommunication equipment providers do not have their own specific NAICS code, an assumption had to be made to use "NAICS 517" pertaining to telecommunication companies. TRD assumes the majority of the costs associated to service and expand the broadband telecommunication facilities in the state are transferred to the end users. The estimated impact for FY17 throughout FY20 was obtained by applying gross receipts growth rate from the December 2015 Consensus Revenue Estimating Group.

This bill may be counter to the LFC tax policy principle of adequacy, efficiency and equity. Due to the increasing cost of tax expenditures revenues may be insufficient to cover growing recurring appropriations.

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) oftax expenditures.

POLICY IMPLICATIONS

The bill would effectively make the construction of nearly all telecommunications facilities, including some used for cable television, eligible for deduction of all gross receipts and compensating tax.

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[1] "*A Broadband Network Cost Model: A basis for public funding essential to bringing nationwide interoperable communications to America's first responders*" Omnibus Broadband Initiative, Technical Paper No.2 Federal Communications Commission. May 2010

According to information from Broadbandnow.com, New Mexico ranks 37th among the states for connectivity. Notably, however, 75 percent of New Mexicans already have broadband access at speeds higher than indicated in the proposed bill. Fiber optic wired coverage remains low at 7.5 percent, however, New Mexicans' access to wired connections at speeds of at least 10 mbps has improved from 72.8 percent to 83.5 percent since 2011. TRD suggests that from a policy perspective, consideration should be given to the 10 megabits per second of download speed and 1 megabit per second of upload speed. They do not appear to conform to the measure of what constitutes high-speed deployment currently used by the FCC. That standard is 25 megabits per second downstream and 3 megabits per second upstream.

While the fiscal impact of this bill is substantial, it does not take into account the potential economic benefits of incentivizing broadband deployment more widely throughout the state. A study by Cornell University[2] that evaluated the economic impact of broadband adoption on rural areas concluded that rural counties with broadband adoption rates higher than 60 percent in 2010 had significantly higher median household income growth rates than those that did not. The authors also found that unemployment rates in the high-adopting counties were lower during and after the recession. Conversely, the study found that counties with broadband adoption rates below 40 percent attracted fewer new businesses and subsequent jobs.

ADMINISTRATIVE IMPLICATIONS

TRD indicated in its analysis of the original bill that the CRS program documentation will need to be updated, but that the costs associated with the change can be absorbed with semi-annual review of the tax program documentation. Taxpayer education may need to be considered to the specific group which is impacted by this change. Auditors will need to be trained in how to inspect records to make sure this is being applied correctly. Overall staff will need to have a general knowledge in order to answer questions.

The IT administrative costs for TRD will include a non-recurring expense of approximately $14,000 in FY16 to establish a location code.

TECHNICAL ISSUES

According to TRD, the term "components" should be defined, as it is a broad term and a lack of definition could result in it being applied too widely.

Also, the deduction from compensating tax for services is unnecessary due to the nature of that tax. Compensating tax is imposed on the purchaser of services only when those services were initially not subject to gross receipts tax, but should have been due to the buyer's subsequent use of those services. In this case, because of the deduction from gross receipts tax, these services would not be subject to the compensating tax to begin with.

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[2] "*Broadband's Contribution to Economic Health in Rural Areas,*" Research and Policy Brief Series, Issue Number 64, Community and Regional Development Institute, Cornell University, February 2015.

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL

If the bill is not enacted, overall project costs for Century Link and Frontier will be higher. However, the companies have already accepted the funding and presumably have committed to completing the projects. More broadly, however, the absence of a more robust broadband network in New Mexico may have the unintended consequence of discouraging new businesses from locating here and of hindering overall economic growth.

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