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FISCAL IMPACT REPORT

SPONSOR <u>Block/Lord/Mirabal Moya</u>	LAST UPDATED _____
	ORIGINAL DATE <u>1/23/2024</u>
SHORT TITLE <u>Firearm & Ammo Gross Receipts</u>	BILL NUMBER <u>House Bill 79</u>
	ANALYST <u>Graeser</u>

REVENUE* (dollars in thousands)

Type	FY24	FY25	FY26	FY27	FY28	Recurring or Nonrecurring	Fund Affected
GRT (Direct cost of Deduction)		(\$3,500.0)	(\$3,600.0)	(\$3,700.0)	(\$3,9800.0)	Recurring	General Fund
GRT (direct cost of deduction)		(\$2,300.0)	(\$2,400.0)	(\$2,400.0)	(\$2,500.0)	Recurring	Local Governments
Hold Harmless		(\$2,300.0)	(\$2,400.0)	(\$2,400.0)	(\$2,500.0)	Recurring	General Fund
Hold Harmless		\$2,300.0	\$2,400.0	\$2,400.0	\$2,500.0	Recurring	Local Governments

Parentheses () indicate revenue decreases.

*Amounts reflect most recent analysis of this legislation.

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT* (dollars in thousands)

Agency/Program	FY24	FY25	FY26	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
TRD	\$132.0	\$3.5	\$0	\$135.5	Nonrecurring	General Fund

Parentheses () indicate expenditure decreases.

*Amounts reflect most recent analysis of this legislation.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

A list of firearms-related bills follows:

HB46, HB47, HB78, HB79, HB88, HB101, HB114, HB127, HB129, HB137, HB168, SB5, SB69, SB90, SB198 and SJR12. Of these, only this bill, HB81 and SB90 are tax related.

Sources of Information

LFC Files

Agency Analysis Received From
Taxation and Revenue Department (TRD)
Department of Public Safety (DPS)

SUMMARY

Synopsis of House Bill 79

House Bill 79 (HB79) proposes a 25 percent gross receipts tax deduction for receipts from the sale of firearms or ammunition. In innovative fashion, local governments are held harmless from this deduction with a new section of statute. Municipal distributions would be increased by the sum of total gross receipts tax local options plus 1.225 percent state share applied to the claimed deductions for that municipality. County distributions would be increased by total gross receipts tax local option tax rates applied to the claimed deductions for that county (separately applied to county rates applicable in municipalities and county remainder areas).

The deduction must be separately reported and TRD is required to include the cost of the deduction in the annual Tax Expenditure Report.

The effective date of this bill is July 1, 2024. There is no sunset date which would allow the Legislature to review the proposal.

FISCAL IMPLICATIONS

This bill creates a tax expenditure. 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) of tax expenditures. LFC has serious concerns about the substantial risk to state revenues from tax expenditures and the increase in revenue volatility from erosion of the revenue base.

TRD has provided the following analysis:

Estimated Revenue Impact*					R or NR**	Fund(s) Affected
FY24	FY25	FY26	FY27	FY28		
--	(\$3,100)	(\$3,200)	(\$3,300)	(\$3,400)	R	Section 1: General Fund Hold Harmless
--	\$3,100	\$3,200	\$3,300	\$3,400	R	Section 1: Local Governments - Hold Harmless
--	(\$2,700)	(\$2,800)	(\$2,900)	(\$3,000)	R	Section 2: General Fund – GRT Deduction
--	(\$1,800)	(\$1,900)	(\$1,900)	(\$2,000)	R	Section 2: Local Governments – GRT Deduction

Per information released by the Alcohol and Tobacco Tax and Trade Bureau on the amount of federal firearms and ammunition excise tax (FAET) collected¹ and the Bureau of Alcohol, Tobacco, Firearms and Explosives data on registered weapons,² the Taxation

¹ <https://www.ttb.gov/tax-audit/tax-collections>

² <https://www.atf.gov/firearms/docs/report/2021-firearms-commerce-report/download>

and Revenue Department (TRD) estimated the FAET paid by New Mexicans. Using an average federal excise tax on producers and importers,³ the economy-wide markup, and assuming taxes on producers are fully passed through to prices,⁴ TRD calculated the tax base for firearms and ammunition in New Mexico. The fiscal impact used the gross receipts tax (GRT) revenue growth from the December 2023 Consensus Revenue Estimating Group (CREG) forecast and is based on the effective statewide gross receipts tax rate.

Confirming TRD’s analysis, LFC staff created a plausible argument:

The industry trade association Safehome.org⁵ estimates 172,990 firearms were sold in New Mexico in 2022 – approximately one percent of all U.S. sales. The National Shooting Sports Foundation⁶ estimates an economic impact (direct, suppliers and induced) of about \$163 million in 2021. It is difficult to determine the value of ammunition from these data.

Assuming an average price of \$700 for new guns, and further assuming 175 percent for ammunition, and an average statewide GRT rate of 7 percent, the approximate Fiscal Impact – imposed totally on the State General Fund -- would be \$5,800.0.

Guns	172,990
\$ per	\$700
	\$121,100,000
Ammunition	\$212,900,000
Total Receipts	\$334,000,000
25 percent deduction	\$83,500,000
Ratio	
Total Rate	7 percent
Cost of deduction	-\$5,800
State Direct Cost	-\$3,500.0
Local Government	-\$2,300.0
Cost	
	= hold harmless

	FY24	FY25	FY26	FY27	FY28
GRT Direct		(\$3,500.0)	(3,600.00)	(3,700.00)	(3,800.00)
Local Gov't Direct		(\$2,300.0)	(2,400.00)	(2,400.00)	(2,500.00)
General Fund Hold Harmless		(\$2,300.0)	(\$2,400.0)	(\$2,400.0)	(\$2,500.0)
Local Gov't Hold Harmless		\$2,300.0	\$2,400.0	\$2,400.0	\$2,500.0

³ The federal excise tax on the import and production of firearms and ammunition is of 10–11 percent.

⁴ In competitive markets taxes are fully passed through to prices. This assumption is supported by the 2,288 US-based firearms and ammunition producers and the fact that these producers have come under considerable import competition pressure not unlike that experienced by other branches of US manufacturing.

⁵ <https://www.safehome.org/data/firearms-guns-statistics>

⁶ <https://www.nssf.org/government-relations/impact>

Although this would be a 1.75 percent reduction in net price, it is unlikely that there would be a distinguishable price elasticity effect. No more guns would be purchased than at present.

SIGNIFICANT ISSUES

This bill narrows the gross receipts tax (GRT) base. Many New Mexico tax reform efforts over the last few years have focused on broadening the GRT base and lowering the rates. Narrowing the base leads to continually rising GRT rates, increasing volatility in the state's largest general fund revenue source. Higher rates compound tax pyramiding issues and force consumers and businesses to pay higher taxes on all other purchases without an exemption, deduction, or credit.

There is no clear purpose for the tax expenditure expressed in the bill. There is little justification in tax policy for this deduction since it may not sustain an industry or preserve jobs.

TRD comments on the policies:

Allowing taxpayers to deduct a part of their tax liability for selling firearms and ammunition could stimulate this sector. Firearms and ammunition manufacturers, distributors, and retailers will lower prices, increase profits, or a mix of both as the tax on these items decreases. If they lower prices, they could experience increased demand. If these businesses become more profitable, more of them may enter the market. A reduction in prices could make firearms and ammunition more accessible, resulting in increased sales.

This bill raises concerns related to public safety, regulation, and gun violence. Reducing tax liabilities and potentially prices on firearms and ammunition could increase gun ownership, which in turn may contribute to an escalation in gun-related accidents and violent crimes. Considering the linkages between legal and illegal markets for firearms and ammunition, a lower price in the formal market will reduce the price in the illegal market also.

GRT rests upon the general presumption that all receipts of a person engaged in business in New Mexico are subject to the gross receipts tax and that this rate represents the rate upon which the State collects taxes on transactions.⁷ GRT represents the largest recurring revenue source for the state General Fund at around 34 percent, about 80 percent of municipal revenue, and 30 percent of county revenue.

While tax incentives may support particular industries or encourage specific social and economic behaviors, the proliferation of such incentives complicates the tax code. Adding more tax incentives: (1) creates special treatment and exceptions to the code, growing tax expenditures or narrowing the tax base, with a negative impact on the General Fund; and (2) increases the burden of compliance on both taxpayers and TRD. Adding complexity and exceptions to the tax code does not comport generally with the best tax policy. Tax incentives are also properly used to stimulate developing markets in goods and services. The firearms industry and market are mature, and there is no

⁷ Section 7-9-3.5(A)(1) NMSA 1978.

evidence that they require economic stimulation.

The hold harmless payments to local governments contained in this bill complicate TRD’s distributions extensively in an effort to shift a relatively small amount of revenue to local governments. The proliferation of new distributions required to be automated in GenTax puts TRD’s mission at risk. Errors in distributions can create costly litigation between the state and local governments. Similarly, local hold harmless payments make filing tax returns more complex for GRT taxpayers, adding risk that taxpayers will file incorrectly and eventually cause revenue clawbacks that can be disastrous to local governments.

The state General Fund currently transfers payments to local governments. Under Section 7-1-6.4 NMSA 1978, State gross receipts tax revenues are already shared with all municipalities. Section 7-1-6.5 NMSA 1978 provides a distribution to the Small County’s Assistance Fund; Section 7-1-6.16 NMSA 1978 provides for a county equalization distribution; and pursuant to Sections 7-1-6.46 and 7-1-6.47 NMSA 1978, distributions are made to certain municipalities and counties, respectively, to offset the cost of food and health care practitioner deductions. In addition, local governments have their own GRT and compensating taxing authority.

PERFORMANCE IMPLICATIONS

The LFC tax policy of accountability is met with the bill’s requirement to report annually to an interim legislative committee regarding the data compiled from the reports from taxpayers taking the deduction and other information to determine whether the deduction is meeting its purpose.

ADMINISTRATIVE IMPLICATIONS

TRD anticipates a moderate implementation cost:

TRD will update forms, instructions, and publications and make information system changes. The new deduction may require an additional publication to fully explain who can claim the deduction and the best way to report the 25 percent as it is not common for gross receipts tax deductions to be based on percentages of the gross receipts from transactions.

TRD’s Administrative Services Division (ASD) anticipates this bill will take approximately 60 hours, split between two existing full-time employees, to be implemented. TRD’s Information Technology Division (ITD) estimates that implementing the bill will require approximately 600 hours or over three months and \$132 thousand of contractual costs.

TRD suggests that the effective date be moved to January 1, 2025, to allow for proper implementation and testing of the changes in the system since the distributions under the bill’s Section 1 add additional complexity to the implementation.

Estimated Additional Operating Budget Impact*				R or NR**	Fund(s) or Agency Affected
FY24	FY25	FY26	3 Year Total Cost		

--	\$3.5	--	\$3.5	NR	TRD – ASD - Operating
\$132.0	--	--	\$132.0	NR	TRD – ITD - Contractual Cost

* In thousands of dollars. Parentheses () indicate a cost saving.

** Recurring (R) or Non-Recurring (NR)

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

A list of firearms-related bills follows:

HB46, HB47, HB78, HB79, HB88, HB101, HB114, HB127, HB129, HB137, HB168, SB198, SB5, SB69, SB90, SB198 and SJR12. Of these, only this bill, HB81 and SB90 are tax related.

At introduction deadline, LFC will provide a detailed listing of the firearms-related bills.

TECHNICAL ISSUES

This bill does not contain a delayed repeal date. LFC recommends adding a delayed repeal date.

TRD suggests four drafting changes:

- The placement of Section 1 should be in the Tax Administration Act and not in the Gross Receipts and Compensating Tax Act. The change will need to be made on page 1, lines 17 and 18.
- TRD suggests changing “January 1, 2024” dates to “July 1, 2024” on page 2, lines 14 and 18 for consistency and to align dates with the effective date of the provision of July 1, 2024.
- TRD is now required by Section 7-1-84 NMSA 1978 to compile and present a tax expenditure budget, which includes the number of taxpayers that claim and the amount of claims for a tax expenditure. Credits and deductions are seen as a tax expenditure and will be included on this report. For that reason, TRD recommends that on page 4, lines 6 through 14 are stricken in full.
- TRD notes that the deduction is applicable to gross receipts taxes, but not compensating taxes. Some sales of firearms and ammunition may be subject to compensating tax, and TRD recommends that any deductions apply equally to both taxes, which are complementary.

OTHER SUBSTANTIVE ISSUES

In assessing all tax legislation, LFC staff considers whether the proposal is aligned with committee-adopted tax policy principles. Those five principles:

- **Adequacy:** Revenue should be adequate to fund needed government services.
- **Efficiency:** Tax base should be as broad as possible and avoid excess reliance on one tax.
- **Equity:** Different taxpayers should be treated fairly.
- **Simplicity:** Collection should be simple and easily understood.
- **Accountability:** Preferences should be easy to monitor and evaluate.

In addition, staff reviews whether the bill meets principles specific to tax expenditures. Those policies and how this bill addresses those issues:

Tax Expenditure Policy Principle	Met?	Comments
<p>Vetted: The proposed new or expanded tax expenditure was vetted through interim legislative committees, such as LFC and the Revenue Stabilization and Tax Policy Committee, to review fiscal, legal, and general policy parameters.</p>	✘	Not Vetted
<p>Targeted: The tax expenditure has a clearly stated purpose, long-term goals, and measurable annual targets designed to mark progress toward the goals.</p> <p style="padding-left: 40px;">Clearly stated purpose</p> <p style="padding-left: 40px;">Long-term goals</p> <p style="padding-left: 40px;">Measurable targets</p>	✘ ✘ ✘	No purpose stated; no goals for reduction in suicides or gun-related violence. Implicit purpose is reducing unsupervised activity.
<p>Transparent: The tax expenditure requires at least annual reporting by the recipients, the Taxation and Revenue Department, and other relevant agencies</p>	✔	Included in the TER
<p>Accountable: The required reporting allows for analysis by members of the public to determine progress toward annual targets and determination of effectiveness and efficiency. The tax expenditure is set to expire unless legislative action is taken to review the tax expenditure and extend the expiration date.</p> <p style="padding-left: 40px;">Public analysis</p> <p style="padding-left: 40px;">Expiration date</p>	✘ ✘	
<p>Effective: The tax expenditure fulfills the stated purpose. If the tax expenditure is designed to alter behavior – for example, economic development incentives intended to increase economic growth – there are indicators the recipients would not have performed the desired actions “but for” the existence of the tax expenditure.</p> <p style="padding-left: 40px;">Fulfills stated purpose</p> <p style="padding-left: 40px;">Passes “but for” test</p>	✘ ✘	No purpose stated; gun sales will not respond.
<p>Efficient: The tax expenditure is the most cost-effective way to achieve the desired results.</p>	✘	
Key: ✔ Met ✘ Not Met ? Unclear		