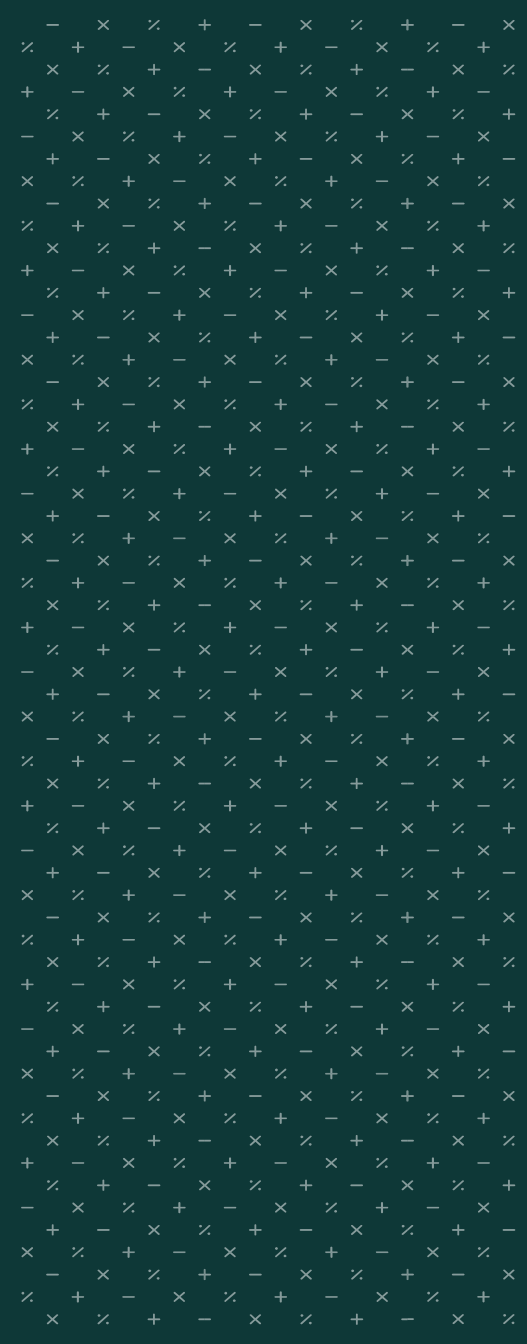




Revenue Stabilization and Tax Policy Committee

Presented by Steven Keene

July 25, 2018



Agenda

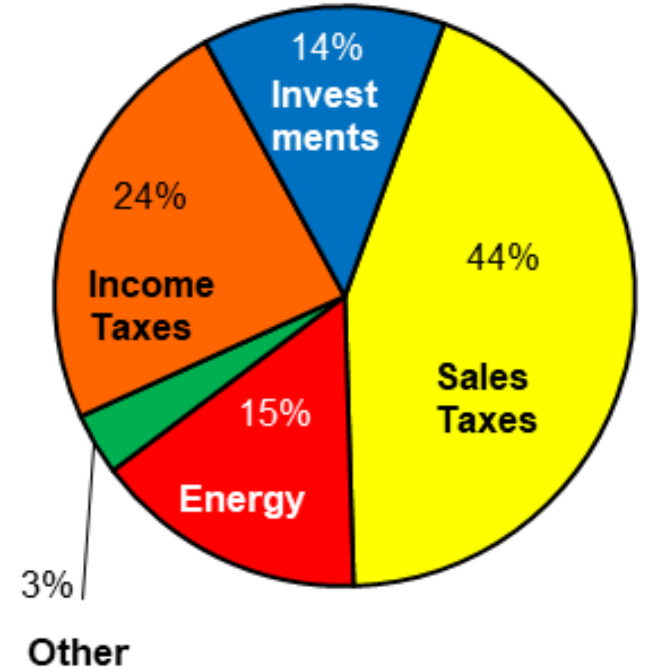
- NMTRI Principles of Good Tax Policy
- Revenue Sources - A few Data Points
- Gross Receipts & Compensating Tax Overview
- Personal Income Tax
- Corporate Income Tax
- Oil and Gas Taxes
- Other Taxes



Estimated Revenue Sources

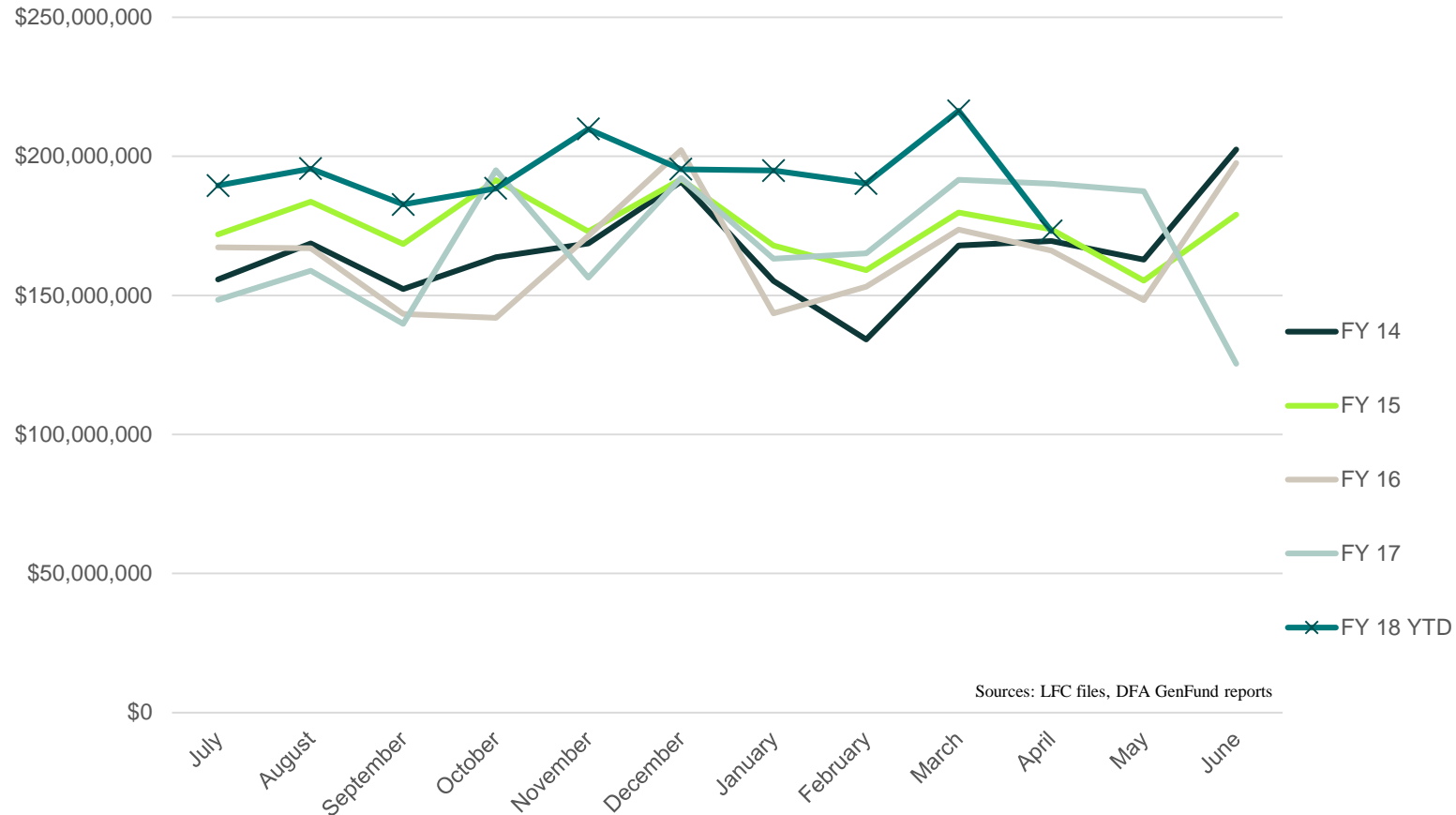
- Taxes on Energy and Combined Sales Tax (GRT makes up the majority of this number) stand out as heavy reliance.
- Property Tax is minimal
- Income Taxes combines Corp and Individual with Individual being the largest component.

**Estimated FY19
General Fund
Revenue Sources**



Source: Jan. 2018 Consensus Revenue Estimate

Gross Receipts Tax Revenues Year-over-Year Comparison

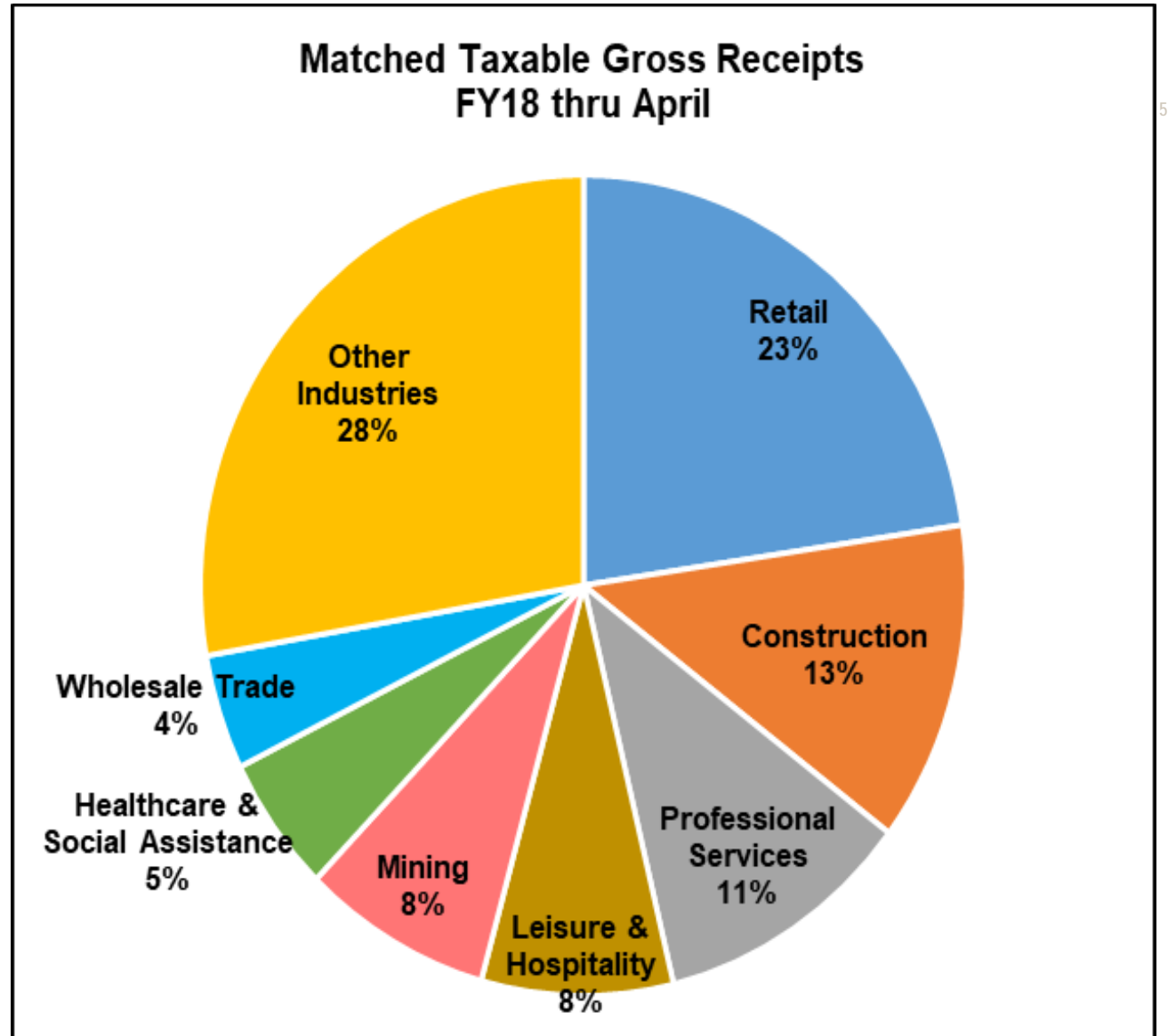


Note: the decline in June 2017 reflects a one time distribution from GRT to PIT Withholding to correct for prior periods.



Industry Receipts

- Retail – could be impacted by Wayfair decision
- Construction is very important
- Industries not typically included in Sales Tax Base:
 - Professional Services
 - Healthcare and Social Assistance



NMTRI Principles of Good Tax Policy

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



How Do New Mexico's Business Taxes Compare?

FY16	New Mexico		United States	
	\$ Billions	TEBTR ¹	\$ Billions	TEBTR ¹
Property Tax	0.9	1.25%	278.1	1.73%
Sales Tax	1.9	2.64%	153.9	0.96%
Excise Tax	0.5	0.70%	89.8	0.56%
CIT	0.1	0.14%	63.2	0.39%
UI Tax	0.3	0.42%	43.1	0.27%
PIT on Business Income	0.1	0.14%	40.3	0.25%
License and Other Taxes	0.7	0.97%	55.6	0.35%
Total Business Taxes	4.6	6.40%	724.1	4.50%

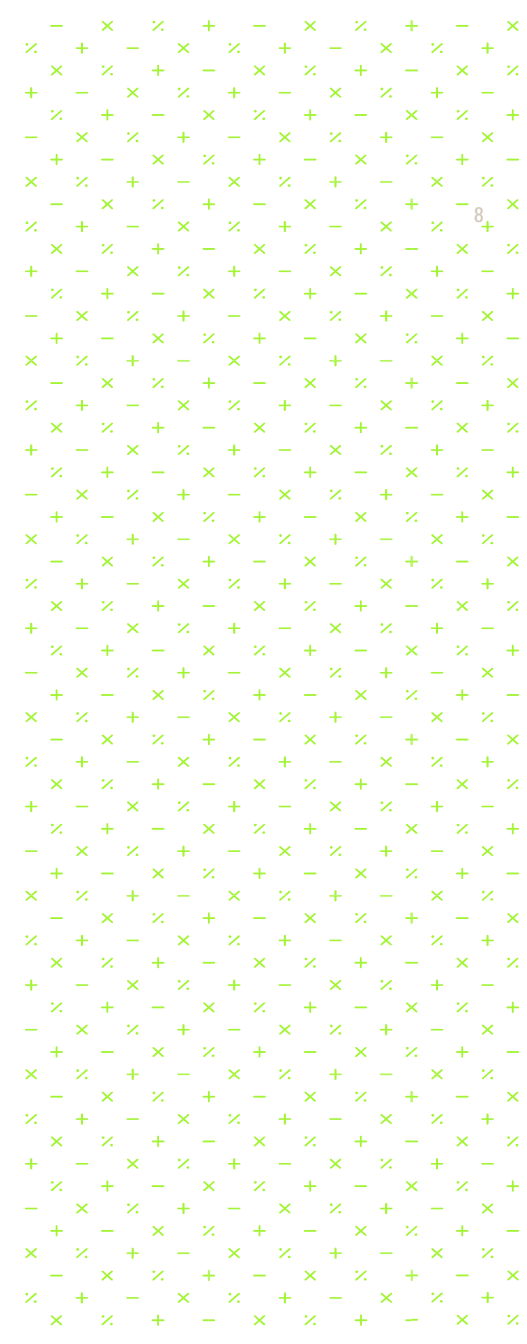
Source: "Total state and local business taxes," Ernst & Young, Council on State Taxation, August 2017.

(1)TEBTR, Total Effective Business Tax Rate is measured as the ratio of state and local business taxes to private-sector gross state product (GSP)





NM Gross Receipts and Compensating Tax



General Fund Revenue Sources – Gross Receipts and Compensating Tax

Imposed in 1935 – “Emergency School Tax”

NM’s largest source of revenue

Broad-based (but less broad over time)

Seller imposed “sales” tax?

Includes services and intangibles

Allows indirect tax on federal government (see *U.S. v. NM*)

Rate includes “local option” taxes imposed by counties, municipalities, and others (i.e. train and spaceport districts)



General Fund Revenue Sources – Gross Receipts and Compensating Tax

State's share = 3.9% (incorporated); 5.125%

GRT rate range: 5% (services only), 5.125% (lowest other GRT rate;); 5.5* to 9.25%* with in-state location

Seller's location determines rate

Except: construction, real estate commissions, utilities

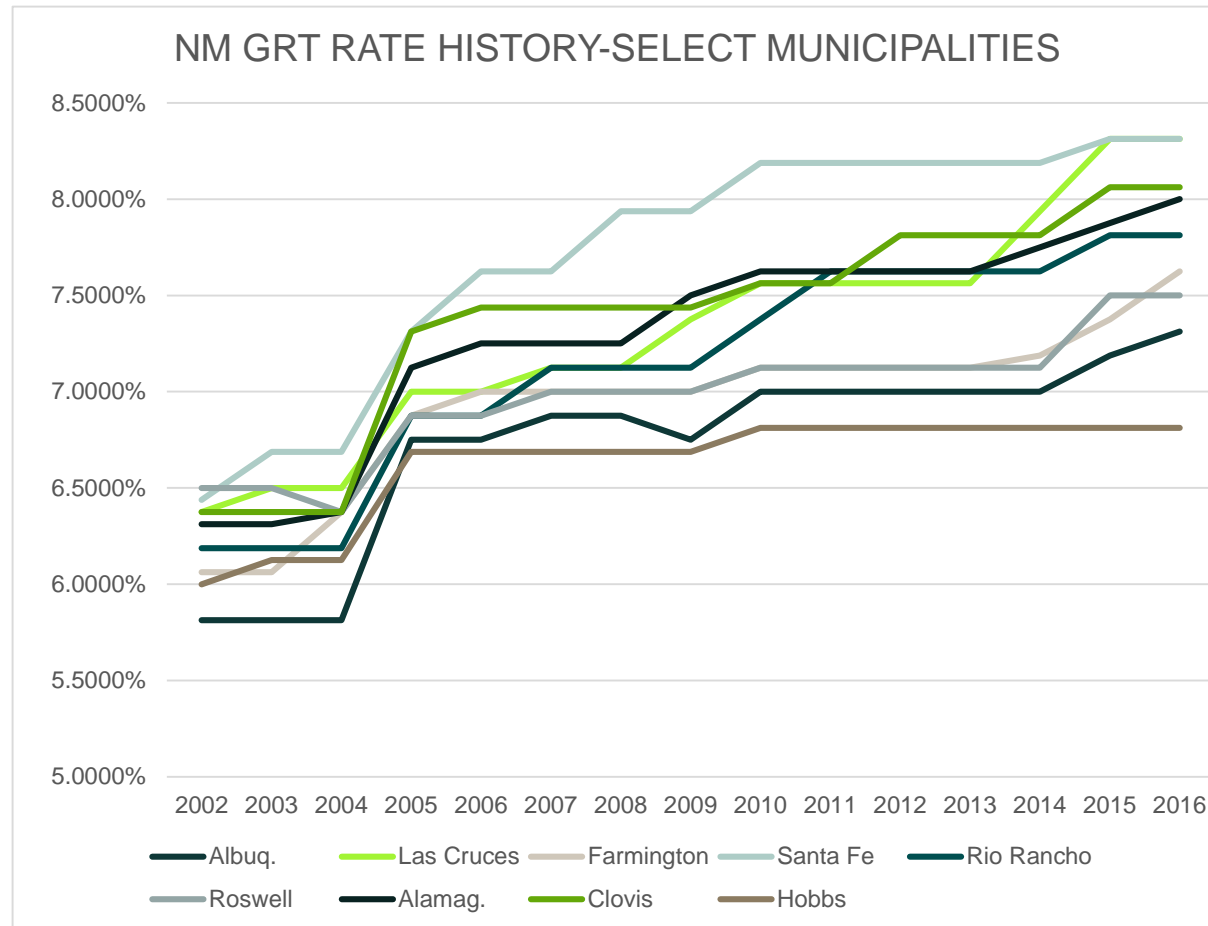
Pyramiding problem: Business-to-Business transactions; “every other sale” taxation of services

“Hold-harmless” features for local government (being phased out)

* Remainder of County – Lea and Lincoln; Taos Ski Valley through 12/18, respectively. Source: NMTRD Rate Schedule.



General Fund Revenue Sources – Gross Receipts and Compensating Tax – Rate Trends



Selected Current Rates

Rates have shown and continual upward trend in the major municipalities.

Mid-sized cities have held rates steady

Rio Rancho has reduced its rate

Municipality		Current Rate	2016 Rate
Albuquerque	↑	7.875%	7.3125%
Alamogordo	→	8%	8%
Clovis	↑	8.1875%	8.0625%
Hobbs	→	6.8125%	6.8125%
Las Cruces	→	8.3125%	8.3125%
Farmington	→	7.625%	7.625%
Roswell	↑	7.8333%	7.5%
Rio Rancho	↓	7.4375%	7.8125%
Santa Fe	↑	8.4375%	8.3125%



General Fund Revenue Sources – Gross Receipts and Compensating Tax – Cont'd

Compensating Tax

- Companion tax (“use” tax) – imposed on purchaser
- In New Mexico – GRT rate differs from comp tax rate
- Municipal and county gross receipts taxes
- Local revenues tightly controlled by Legislature
- Local option taxes
- GRT provides 75% of municipal general revenue
- Bases are identical – so locals piggyback on state base



General Fund Revenue Sources – Gross Receipts and Compensating Tax – Cont'd

Compensating tax

- **Imposed on the value of property**
 - manufactured in the state by the person using it
 - acquired outside NM that would have been subject to the GRT had it been acquired in NM
 - that becomes taxable because of subsequent use of the property or service (i.e. using something acquired for resale)
- **Rate = 5.125% (5% for services)**
 - **Credit for tax (sales) paid to other state up to 5.125%**
- **Exemptions & Deduction mirror GRT where applicable**
- **Doesn't apply to individuals**
- Interstate commerce issue – some sales not taxed
- **Also funds small cities and counties assistance funds**



General Fund Revenue Sources – Gross Receipts and Compensating Tax – Cont'd

Tribal taxes

- Tribal governments are sovereign with respect to the state. They have taxing power of their own.
- They do not have to align their general excise tax with New Mexico's. It is a matter of mutual convenience that they do.
- Currently 15 tribal entities impose a gross receipts tax administered by the state under cooperative agreements.



General Fund Revenue Sources – Gross Receipts and Compensating Tax Exemptions and Deductions

Things that are taxed elsewhere in tax law

- i.e. motor vehicles, insurance, gasoline
- **But not all things (i.e. cigarettes, alcohol, rental cars)**
- Certain sales by and to governments and charitable organizations
- Certain sales in the chain of commerce – to reduce pyramiding
- **(direct sales for resale, some services for resale)**



General Fund Revenue Sources – Gross Receipts and Compensating Tax Exemptions and Deductions

Other things that the legislature thinks shouldn't be taxed

- **Traditionally - wages, dividends and interest, certain intangibles, sale/lease of real property - things that were not intended to be taxed but would otherwise fall within the broad definition of “gross receipts”**
- **Recent Trend – more and more deductions for social, economic development, or other reasons such as food, medical (physicians, for-profit hospitals, medical labs, certain aircraft services, financial management fees, veterinary services or supplies for cattle, boxing/wrestling/kickboxing, certain referees, some construction ; hearing and vision aids, renewable energy, etc.**



General Fund Revenue Sources – Gross Receipts and Compensating Tax – Tax Credits

Tax credits

- Investment
- Lab partnership
- Technology jobs
- High-wage
- Advanced energy
- R&D small business
- Affordable housing
- Alternative energy manufacturing



General Fund Revenue Sources – Gross Receipts and Compensating Tax – Special Definitions

GRT system includes “Special” state taxes

Governmental GRT

- Justified by competition between governments and businesses
- Bucks used for capital outlay projects of select local governments & state agencies
- Could be folded into regular GRT

Interstate telecommunications GRT

- Long-distance service was taxed under the gross receipts tax until 1992
- This separate tax was created, mainly as a convenience to the long-distance companies
- The FCC would not permit passing on the tax unless local rates were part of a special tax
- ITGRT’s rate of 4.25% determined as an average of the actual effective gross receipts tax rate

Lease vehicle GRT & surtax

- At the behest of auto rental companies, this 5% tax on top of regular GRT replaced the motor vehicle excise tax on the same vehicles.
- Effectively reduced interest paid on financed vehicle purchases.
- Tax is targeted at tourists.

Telecommunications relay service surcharge

- Rate = 0.33% - charged on receipts from intrastate telephone services.
- It funds TTY/TDD services.
- It is a special excise tax that happens to be collected through the gross receipts tax system.



General Fund Revenue Sources – Personal Income Tax

NM imposes a personal income tax on residents, and non-residents deriving income from New Mexico sources

The starting point is federal adjusted gross income (AGI) followed by additions and subtractions:

+ NM additions (e.g., interest on federally tax-exempt bonds; itemized state income tax)

- Federal standard or itemized deductions

- Federal personal exemption amount

- NM low- and middle-income exemption

- NM subtractions (e.g., interest on NM state and local bonds, capital gains)

- NM uncompensated medical care deduction

= NM taxable income



General Fund Revenue Sources – Personal Income Tax – Cont'd

Most credits are nonrefundable (but may be carried forward)

Refundable rebates and credits (except the Working Families Tax Credit) are based on “Modified Gross Income” (MGI).

Withholding and estimated payments are applied.

Taxpayers compute their tax due or refund.

Graduated rates that range from 1.7% to 4.9%.

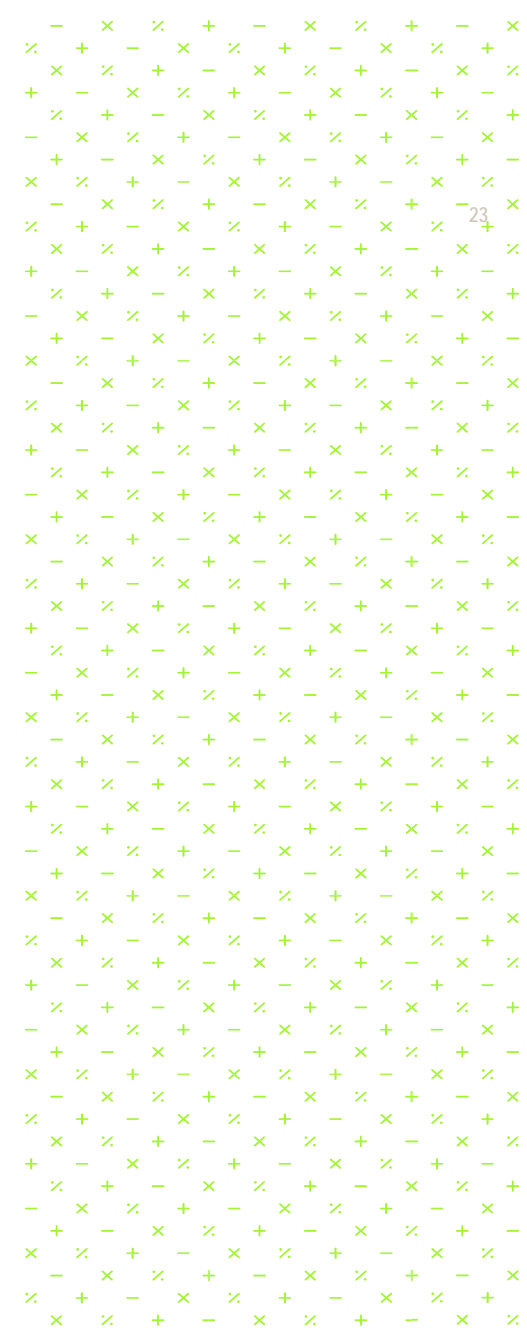
With Top Rate hitting in at relatively low \$24,000 for MFJ

Tax credits and rebates may reduce tax due.





Corporate Income Tax



General Fund Revenue Sources – Corporate Income Tax

Entities Subject to Tax

Corporations

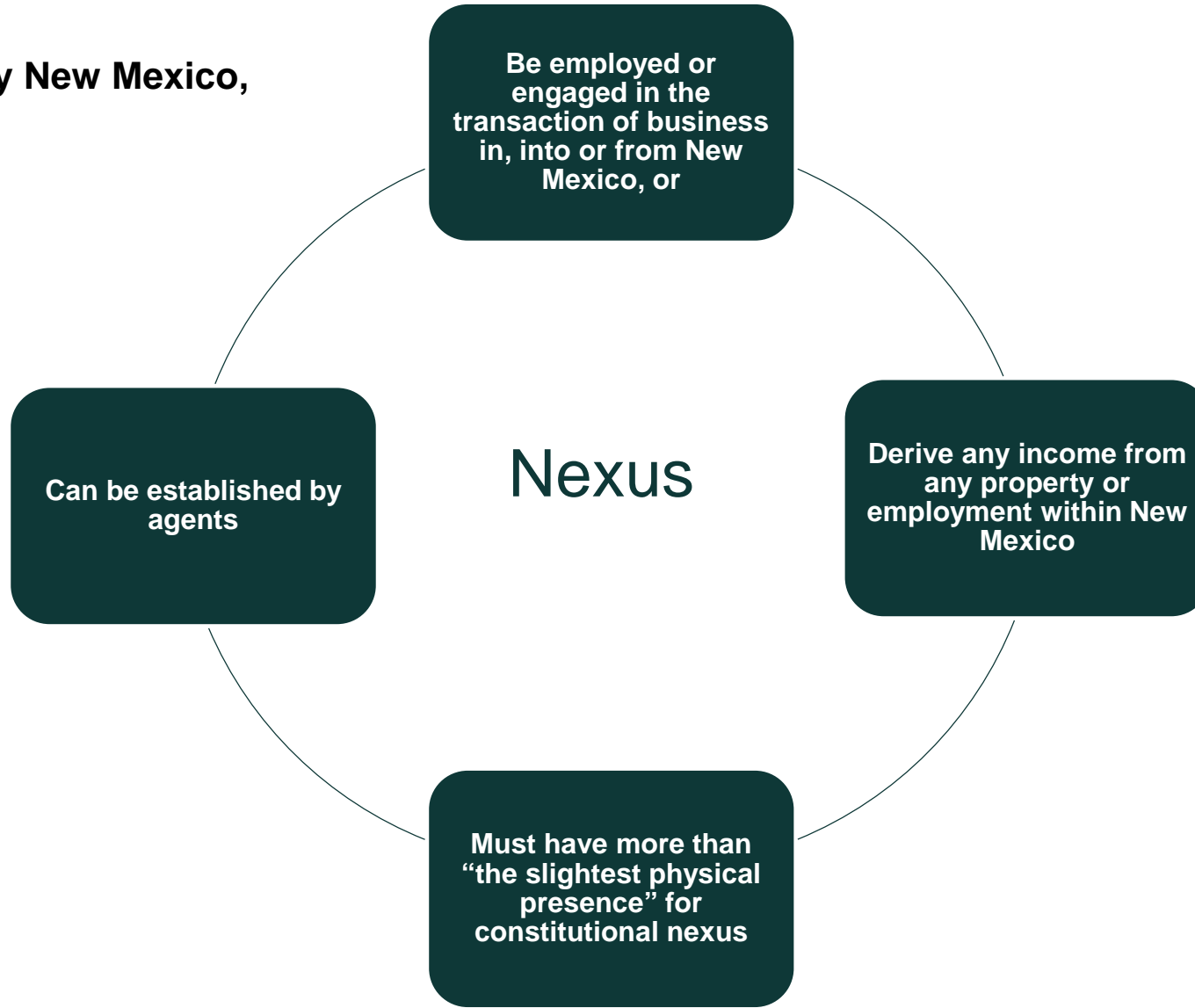
Other entities taxed
as corporations under
federal income tax

Certain partnerships,
LLCs, Non-profits
(i.e. UBI), Trusts



General Fund Revenue Sources – Corporate Income Tax

To be subject to tax by New Mexico, entity must:



General Fund Revenue Sources – Corporate Income Tax – Cont’d

Taxable Income

TAXABLE INCOME AS DEFINED FOR FEDERAL INCOME TAX PURPOSES, WITH CERTAIN ADDITIONS AND SUBTRACTIONS

ADDITIONS:

Interest on non-New Mexico state and local bonds

Federal NOLs (3 year carryback, 20 year carryforward)

SUBTRACTIONS:

Interest on federal bonds and New Mexico state and local bonds subject to federal income tax

State NOLs (no carryback, now 20 year carryforward (was 5 year)

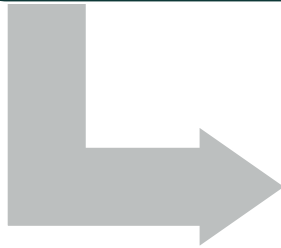
Dividends from foreign corporations (not combined filers, and including “gross-up”; percentage based on ownership)



General Fund Revenue Sources – Corporate Income Tax – Cont’d

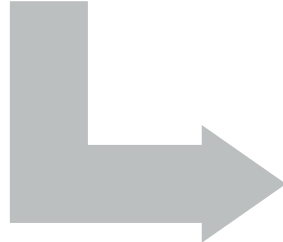
Separate Corporate Entity (SCE)

- Default reporting method, unless taxpayer elects combined or consolidated



Combined

- Can be elected by “unitary” corporations (determined by inter-relations)
- Once elected, cannot go back to SCE without permission of TRD Secretary



Consolidated

- Follows federal rules (requires 80% ownership by common parent)
- Once elected, cannot go back to combined or SCE without permission of TRD Secretary



General Fund Revenue Sources – Corporate Income Tax – Cont’d

Allocation and Apportionment

- **Corporations with income from outside New Mexico must allocate and apportion their income to New Mexico**
- **NM follows Uniform Division of Income for Tax Purposes Act (UDITPA)**
- **“Non-business” income is “allocated” to one state (source state)**
- **“Business income” is “apportioned” between states by formula**
- **Apportionment formula uses 3- “factors” - property, payroll, and sales**
- **Each factor is the percentage of the New Mexico amount to the “everywhere” amount, and the three percentages are then added and divided by 3 to get the average apportionment percentage**

Manufacturers and corporate HQs (or some ops) can elect to use a single sales factor formula that is currently being phased in (which may benefit those who have property and payroll here but sells mostly outside the state).



General Fund Revenue Sources – Corporate Income Tax – Cont’d

Tax Liability

Corporate income tax is imposed at three rates:

4.8% for net income of \$500,000 or less;

5.9% of net income \$500,000 and over

New Mexico corporate income tax rate will be slightly above the average of surrounding states (except CA), and close to national average

In NM, rates are applied to the taxpayer’s unapportioned income, and that tax is then prorated based on the taxpayer’s apportion/allocation percentages

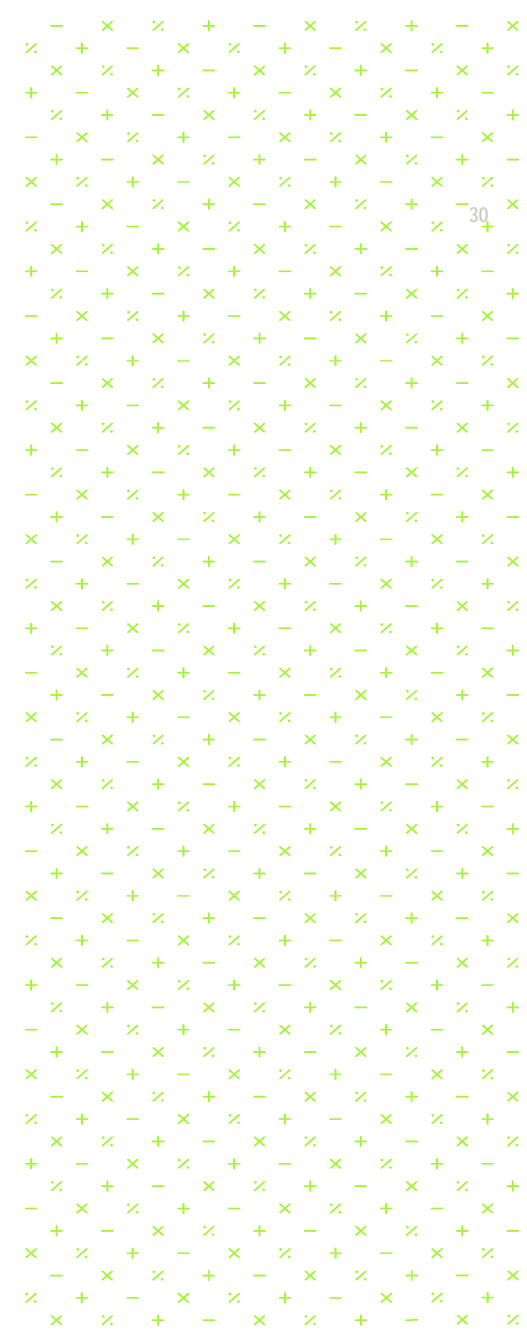
Credits reduce tax liability

Corporate franchise tax also applies - \$50 per year per corporation





Oil and Gas Taxes



Oil and Gas Taxes

Tax rates – Oil

Taxes on Oil	Ordinary Rate	Stripper Wells, Based on Net Price of Oil (\$/bbl)	
		Under \$15	\$15 to \$18
Oil and Gas Emergency School Tax	3.15%	1.58%	2.36%
Oil and Gas Severance Tax ^{1,2}	3.75%	1.875%	2.8125%
Subtotal	6.9%	3.455%	5.1725%
Oil and Gas Conservation Tax ³	0.19%	0.19%	0.19%
Production Ad Valorem Tax ⁴	1.28%	1.28%	1.28%
Total Production Taxes	8.37%	4.925%	6.643%
Production Equipment Ad Valorem Tax ⁵	2.55%	2.55%	2.55%

(1) 2.45% for well workover projects if the average annual WTI price was less than \$24.

(2) 1.875% for qualified enhanced recovery projects if the average annual WTI price was less than \$28.

(3) 0.24% if the average WTI price over the previous quarter was over \$70.

(4) Average effective rate. Ad Valorem rates vary by location.

(5) Average rate. Applied against taxable value of production x uniform assessment ratio (1/3).

Note: Deductions allowed for state, federal and Indian royalties and trucking expenses - In FY 2008, for natural gas averaged 19.18%.



Oil and Gas Taxes

Tax rates – Natural Gas

Taxes on Natural Gas	Ordinary Rate	Stripper Wells, Based on Net Price of Natural Gas (\$/mcf)	
		Under \$1.15	\$1.15 to \$1.35
Oil and Gas Emergency School Tax	4.0%	2.00%	3.00%
Oil and Gas Severance Tax¹	3.75%	1.875%	2.8125%
Subtotal	7.75%	3.875%	5.8125%
Oil and Gas Conservation Tax²	0.19%	0.19%	0.19%
Production Ad Valorem Tax³	1.28%	1.28%	1.28%
Total Production Taxes	9.22%	5.345%	7.2825
Production Equipment Ad Valorem Tax⁴	2.55%	2.55%	2.55%

(1) 2.45% for well workover projects if the average annual WTI price was less than \$24.

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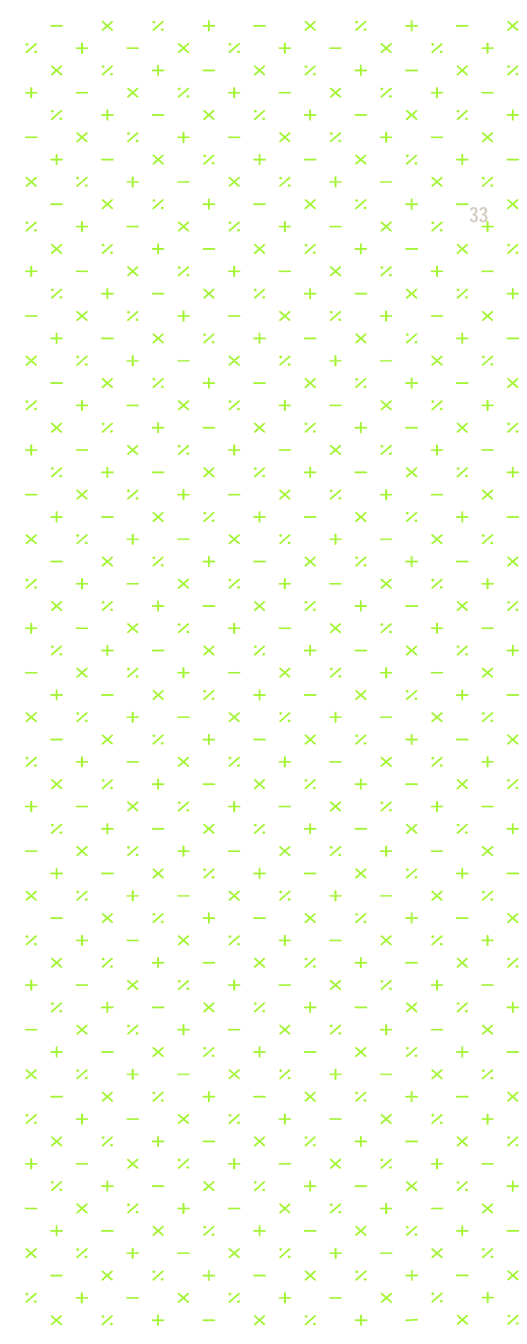
Note: Deductions allowed for state, federal and Indian royalties and trucking expenses - In FY 2008, for natural gas averaged 19.18%.





MOSSADAMS

Other Taxes



Selective Sales Taxes – Tobacco

Cigarettes

- \$1.66 per pack of 20 cigarettes
- Tax raised from \$.21 to \$.91/pack of 20 on July 1, 2003 and again to the present rate on July 1, 2010
- Requires stamps
- **Exemptions**
 - U.S. or any agency thereof
 - governing body or enrolled member of any tribe for sale or use on that tribe or pueblo
 - sales prohibited by N.M. or U.S. constitution

Tobacco Products Tax (snuff, cigars, etc.)

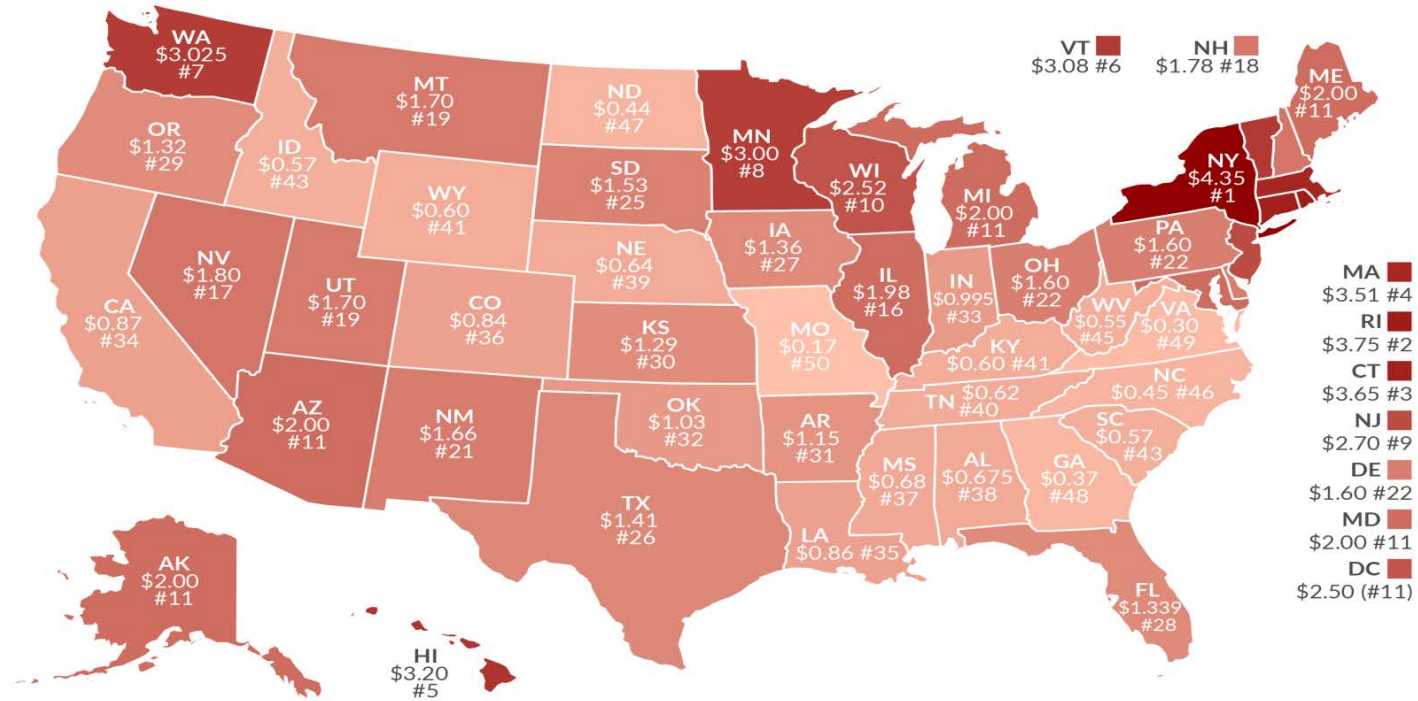
- 25% of product value
- **Exemptions**
 - Products sold to or by the U.S. or N.M., or any of their agents or instrumentalities
- **Deductions**
 - Interstate sales



Selective Sales Taxes – Tobacco

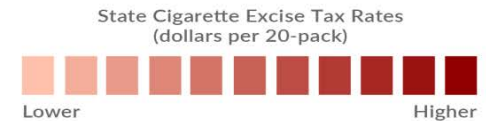
How High Are Cigarette Taxes in Your State?

State Cigarette Excise Tax Rates as of Jan. 1, 2016 (dollars per 20-pack)



Note: Local taxes are not included and can be substantial. D.C.'s rank does not affect states' ranks, but the figure in parentheses indicates where it would rank if included.

Source: Tax Foundation; RJ Reynolds; state revenue departments.



Selective Excise Taxes - Liquor

Rates vary by type

- Spirituous Liquor - \$1.60/liter
- Beer - \$0.41/gallon
- Wine - \$0.45/liter
- Fortified Wine - \$1.50/liter
- Microbrewer beer- \$0.08/liter for the first 10k barrels produced, \$0.28 per gallon for all barrels over 10k but fewer than 15k
- Small winery or winegrower - \$0.10/liter up to 80K liters; \$0.20/liter on amounts over 80K liters but less than 950K liters; \$0.030/liter on amounts over 950k liters but less than 1.5M liters
- Cider - \$0.41/gallon

Exemptions

- Sales to or by instrumentality of the armed forces engaged in resale

Deductions

- Interstate sales



Selective Sales Taxes - Insurance

Administered by Insurance Division of the Public Regulation Commission (PRC)

- **Tax on Premiums**
- Tax rate – 3.003%
- **Imposed in lieu of all other state taxes except property taxes**

Health Insurance Premiums Surtax

- Imposed on health insurance premiums
- Tax rate – 1.00%

Other issues – Retaliatory taxes

- Many states, to include NM, have provisions impose a retaliatory tax on foreign insurers if that insurer's home state's rates are higher than their own rates.



Selective Sales Taxes - Gaming

Gaming Taxes

GAMING TAX

Administered by the Gaming Control Board

- 10% of receipts from sale or lease or other transfer of game devices
 - Exception for transfer from manufacturers to distributors
- 10% of the net take of a gaming operator that is a not-for-profit
- 26% of the net take of other gaming operators
- In lieu of other state and local gross receipts taxes

GAMING OPERATOR THAT IS A RACETRACK

Administered by the Racing Commission

- 20% of net take to purses (in addition to gaming tax)



Used To Be ...

Who to
tax?



Old School

In March 1932 “Collier’s Weekly” ran an article titled “Tax Everyone But Me” which included an instance starting with “Congress! Congress! Don’t tax me” instead of the sing-song: “Don’t tax you. Don’t tax me”.

“Most people have the same philosophy about taxes,” says Senator Russell B. Long, who has heard all the variations during seven years as chairman of the Senate Finance Committee, which handles tax legislation. Long puts that universal theme to verse:

At the end of the year, and again at the opening of 1932, the hotel rooms and lobbies of Washington were crowded and swarming with citizens who had come to play, in paraphrased adult form, an old game of their childhood:

***Don’t tax you,
Don’t tax me,
Tax that fellow behind the tree.***

Congress! Congress! Don’t tax me,

Tax that fellow behind the tree.



New School



41



<https://www.crazygames.com/game/dont-tax-me-bro>

