

Tax Expenditure's; Reporting and Evaluation

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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

What is a “Tax Expenditures”

- Congressional Budget Act of 1974:
 - *“revenue losses attributable to provisions of the federal tax laws which allow a **special** exclusion, exemption or deduction from gross income or which provide a **special** credit, a preferential rate of tax, or a deferral of tax liability.” (emphasis added)*
- In order to implement the requirement to provide a report on tax expenditures, the Congressional Joint Committee on Taxation has defined a “normal income tax structure” against which they compare provisions to identify those that reduce revenue.
- The U.S. Treasury Department has developed a “Reference Tax Law” approach to Tax Expenditures in which provisions are compared to the basic structure of the tax. Focus is often on provisions that benefit a limited number of taxpayers.

Defining a “Normal” Tax Structure

- Income Taxes:
 - Should the tax base be income or consumption?
 - Should the tax rate structure be progressive, proportional or regressive?
 - How should appropriate deductions be determined for expenses like depreciation?
 - Should Corporations be taxed as well as individuals?
- Sales Taxes:
 - Should the base be Broad-based Consumption, Value Added Tax (“VAT”) or some hybrid?
 - Should business purchases – other than for re-sale -- be included in the normal tax base?
- Gross Receipts Tax (NM) – What’s the “normal” base
 - You can’t define a tax expenditure without defining the normal base
 - We tend to view in the context of a an “ideal” broad based sales tax, but was initially viewed more broadly, but never as a true GRT

Exemptions, Deductions and Credit's – oh my!

- Exemptions, deductions, and credits in the context of the GRT have a meaning but tend to be construed together
 - Not all provisions are necessarily properly classified presently
- Even so, they tend to be scored in TER's similarly and viewed as giveaways that can be recaptured by policy maker's
 - Certainly not always the case
 - List's of tax expenditures can't be footed
 - Timing issues and overlapping provisions muddy the water
- Static or broader scores don't necessarily identify all costs and benefits to the state and others
 - More in-depth analysis necessary, but
 - Costly
 - Subjectivity increases, as does uncertainty

Tax Expenditure Analysis

- Most experts agree more extensive analysis is warranted in some cases
- Simply requiring more broad detailed reporting isn't always the answer.
 - But in some cases much more information is required.
- If additional information is desired, more financial resources need be invested in the evaluation process and the process itself requires thoughtful consideration
 - Which tax expenditures require additional evaluation and how often?
 - Where should the evaluation function be housed?
 - TRD (tax research, IG, taxpayer advocate), EDD, LFC, other?

Closing Thoughts

- Don't assume all exemptions/deductions/credits are created equally
- Better analysis is necessary as are greater resources
 - Pick and choose the most needed analysis and fund the efforts
 - Don't impose requirements that burden taxpayers
- Perfect answers to any these question will never be found
 - We'll always end up having to deal with imperfect information
 - Better answers can be found
- Best practices are being developed by other states, the Pew Institute, and others that should be reviewed and evaluated on an ongoing basis

QUESTIONS?