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Gross Receipts Tax Exemption for Broadband Infrastructure - New Mexico

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Taxing Business-to-Business Sales

- When a state taxes purchases of goods and services or business-to-business sales that become part of a final consumer good = taxing "business inputs"

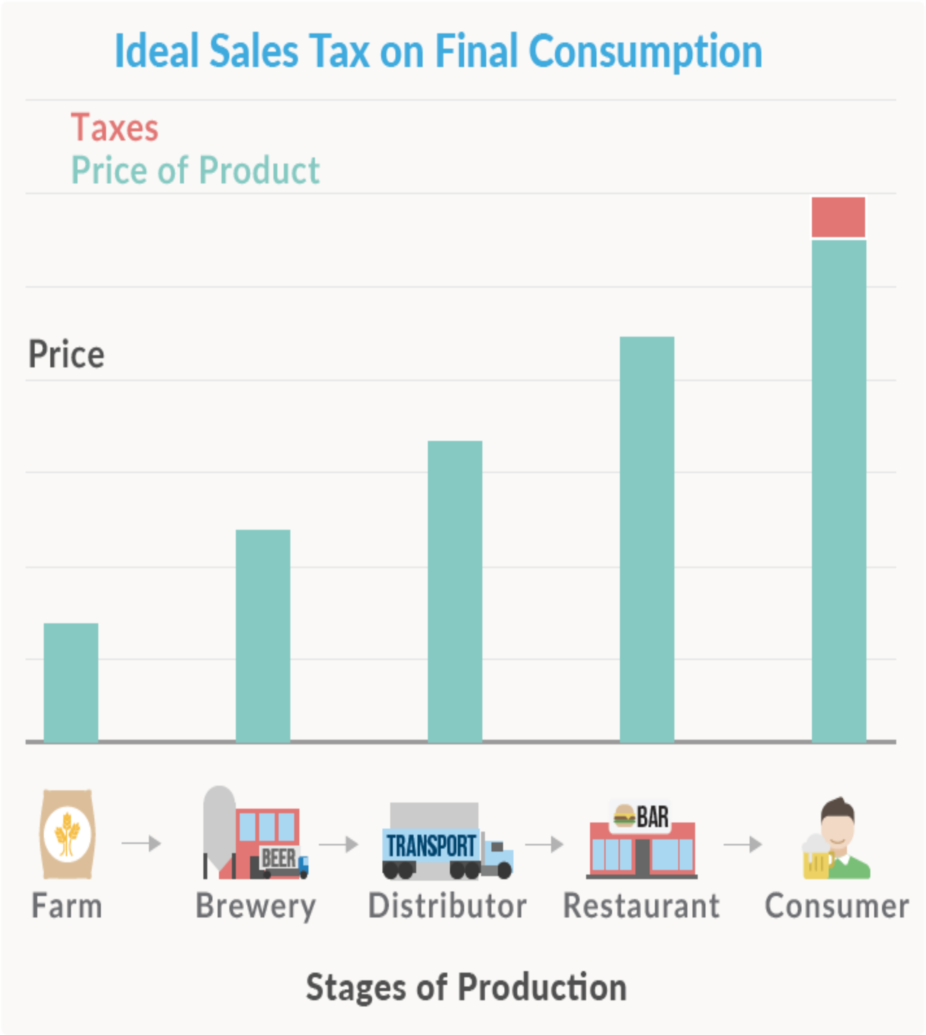
- Taxing business inputs = BAD TAX POLICY

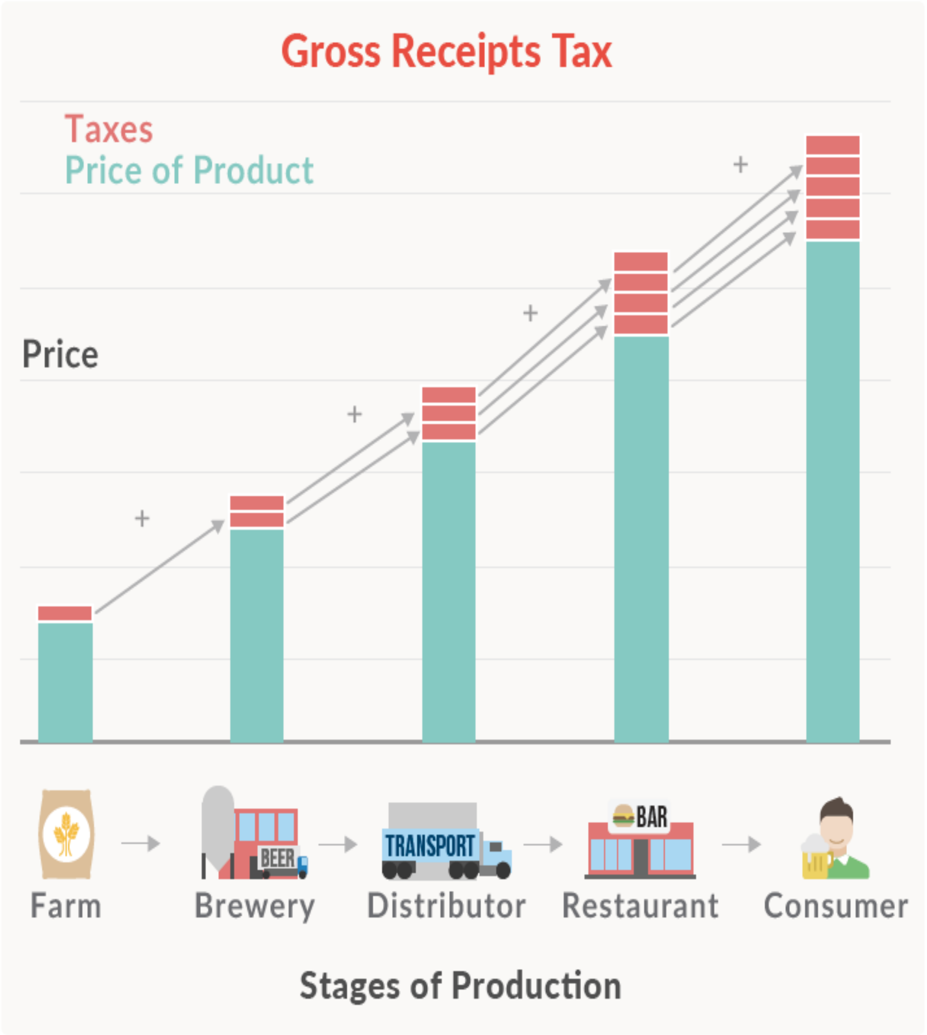
- Creates "tax pyramiding" = situation where sales tax is imposed multiple times on the same value of business input purchases at multiple stages of the production and distribution process leading up to a final sale to consumers

- Because of the multiple times tax is assessed on the item, tax pyramiding results in an effective (real) sales tax rate higher than the statutory tax rate

- Creates a lack of transparency because the final consumer doesn't know exactly how much they paid for taxes v. the product

Tax Pyramiding Illustration





Taxing Business-to-Business Sales

Impact to New Mexico –

- additional cost of doing business in the state
- companies must either attempt to pass on the added layers of tax to their customers or REDUCE THEIR ECONOMIC ACTIVITY IN THE STATE
- Also, New Mexico companies put at a COMPETITIVE DISADVANTAGE to many of their competitors and in foreign markets
    - Example: In NM, the GR tax does not impose use tax on the purchaser of taxable services from out-of-state suppliers but that purchaser is subject to use tax if they purchase taxable services from an in-state supplier; makes NM companies less competitive in foreign markets

New Mexico Observations

- Tax Foundation 2017 “Facts & Figures” observations re NM;
  - #5 for the breadth of their sales/GR tax
  - #9 for state reliance on sales/GR taxes
  - #42 worst state business tax climate for sales/GR tax
  - the sales/GR taxes in HI, New Mexico and SD have broad bases that include many services

- Council on State Taxation (COST), Ernst & Young observation:
  - New Mexico ranks #2 for the extent to which they impose taxes on business inputs

Lack of Parity With Manufacturing Industry

- Currently, about 47 states provide a sales/GR tax exemption for manufacturing equipment; whereas, only about 21 states provide the same exemption for telecommunications equipment

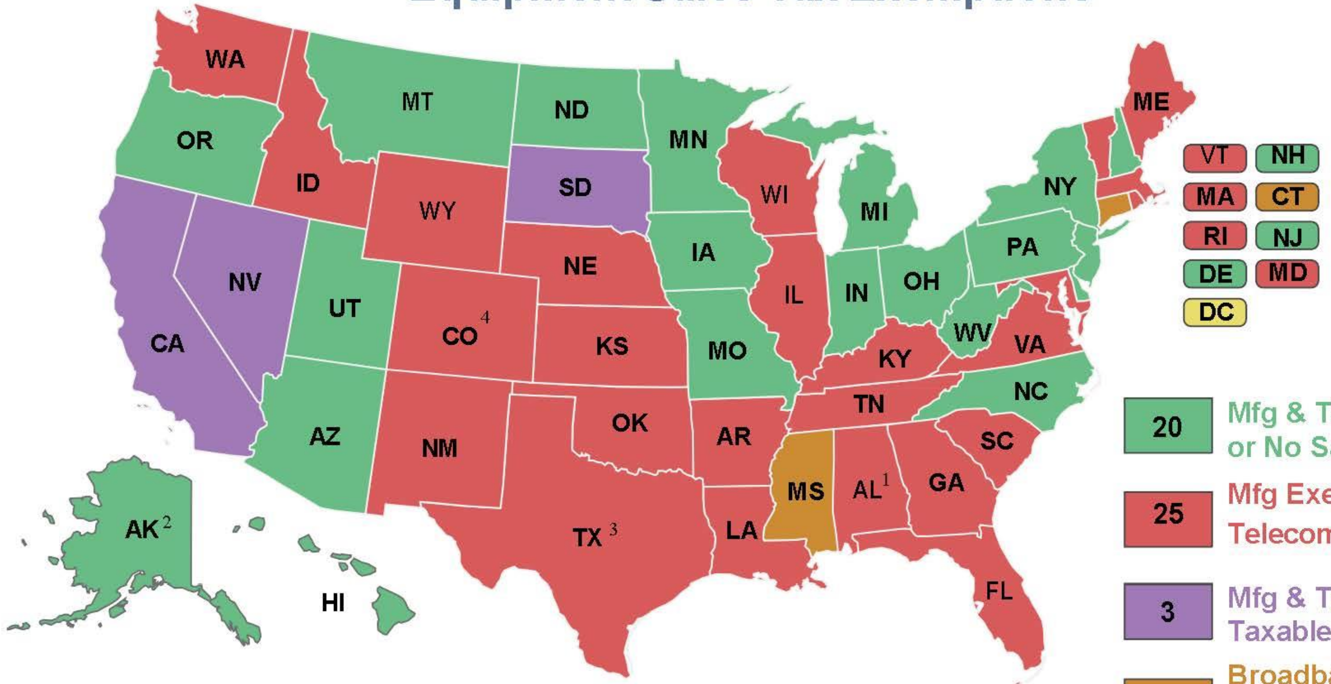
- NEED A TAX EXEMPTION FOR COMMUNICATIONS EQUIPMENT, LIKE THE MANUFACTURING INDUSTRY ENJOYS

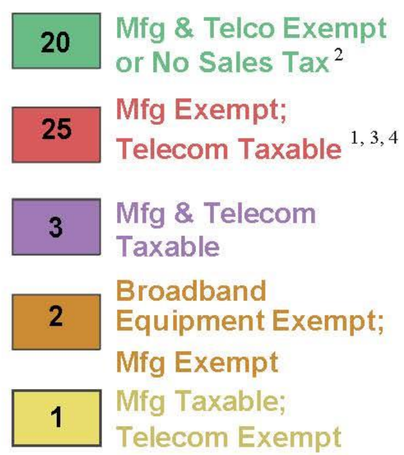
- Both industries = capital-intensive, so WHY THE DIFFERENT TREATMENT???

- Typical capital planning for communications:
  - maintenance of existing plant,
  - network modernization, and
  - capacity upgrades

Equipment Sales Tax Exemption

Telecommunications/Manufacturing Equipment Sales Tax Exemptions





1 Alabama - special reduced 1.5% rate

2 Alaska - local sales taxes may apply

3 Texas - rebate of taxes paid capped at $50 million

4 Colorado - rebate of taxes paid capped at $1 million

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Raul Katz Study: GR Rate Decreases - Increased Investment

<u>NORTH DAKOTA</u>

- Eliminated sales tax for communications equipment in 2009 that impacted 2010 investment

- In 2010, there was a MAJOR increase in the level of investment by wireless and wireline companies of **207%**, as well as increases by CenturyLink since that time

- Consequences of rate decrease:
  - state sent a message to operators regarding the attractiveness of conducting business in that particular state
  - the money saved in taxes flowed to investment
  - the funds that could have been invested in other states, now tend to flow to the state that has reduced its sales tax

Raul Katz Study: GR Rate Decreases - Increased Investment

IOWA

- adopted a progressive sales tax reduction from 4.71% to 1.86% between 2006 and 2010
- effect of rate reduction on wireless and wireline investment was less accentuated than in ND
- Rate reduction between 2006-2010 resulted in a 37% increase in investment, as well as increases by CenturyLink since that time
- Implications = cumulative effect of yearly rate decreases had reached a point where wireless and wireline industries could confidently increase their level of investment

Raul Katz Study: GR Rate Increases – Decreased Investment

SOUTH CAROLINA

- Sales tax rate increased significantly b/t 2006 and 2007, from 6.25% to 7.25%
- Resulted in a large contraction in the level of investment, which decreased 33%

MASSACHUSETTS

- 25% increase in the sales tax rate (from 5.0% to 6.25% in 2010) resulted in a reduction in investment b/t 2009 and 2010

Raul Katz Study: Overall Conclusions (2012)

- As the models indicate, investment in telecommunications is sensitive to sales taxes
- A decrease of 1% in the average sales tax rate results in an increase in telecommunications carrier investment by $263 million per year
- Total elimination of the sales tax affecting the purchase of equipment for telecommunications in the states that currently impose such taxes could increase economic growth by $33 billion and lead to the creation of 243,000 jobs in 3 years
- New economic activity will generate substantial offsetting revenues for state and local governments as new employment and economic activity generates income, sales, property, and other tax revenue for governments

Recap

- Exempting broadband infrastructure from the gross receipts tax in New Mexico will result in increased broadband investment by telecommunications companies which will benefit New Mexico in the following ways:
  - Creating jobs and new and increased economic opportunities
  - Ensuring that citizens and businesses in NM have access to the most technologically advanced services
  - Improving the rural quality of life and economy through things like distance learning, telemedicine, etc.
  - Increasing state and local tax revenues for the future, through the increased size of NM's economy

Forbes excerpt:

"*Yet, as the Council On State Taxation has found, business entities pay about half the sales tax in the United States. This is one of the clearest cases of needed tax reform. There will be several proposals to eliminate the sales tax on business purchases in the coming legislative sessions. Legislators would be wise to enact them. This is not a left or right issue. Indeed, The Tax Foundation, the Center on Budget and Policy Priorities, and virtually everyone else who has ever studied the matter agrees that taxing business inputs is unwise.*"

~Forbes magazine, Jan 2014

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