LEGISLATIVE EDUCATION STUDY COMMITTEE
BILL ANALYSIS

Bill No: SB 389 **49th Legislature, 1st Session, 2009**

Short Title: Corporate Tax to Public School Fund

Sponsor(s): Senator Peter Wirth and Others

Analyst: Kathleen Forrer **Date: March 16, 2009**

Bill Summary:

SB 389:

- amends the *Corporate Income and Franchise Tax Act* to require a unitary corporation subject to taxation under the act to file a combined report with other unitary corporations;[1] and
- repeals a section of the *Corporate Income and Franchise Tax Act* to eliminate consolidated corporate income tax returns; and
- adds a new section to the *Tax Administration Act* to require that 16.66 percent of the net receipts attributable to the Corporate Income Tax be distributed to the Public School Fund.

The provisions in the bill are applicable to taxable years beginning on or after January 1, 2009.

Fiscal Impact:

SB 389 makes no appropriation.

The bill designates 16.66 percent of the receipts attributable to the corporate income tax for distribution to the Public School Fund.

Fiscal Issues:

The Taxation and Revenue Department (TRD) estimates that mandating combined filing would increase New Mexico's corporate income tax revenues by 20 percent of the consensus forecasts for "pre-credit" corporate income tax revenues but also notes that the "volatile nature" of corporate earnings makes this particular forecast less certain than other revenue forecasts provided to the Legislature. In dollar terms, TRD estimates that the changes mandated in SB 389 would result in increased revenue of $94.7 million in FY 10; $69.8 million in FY 11; $77.6 million in FY 12; and $85.4 million in FY 13.

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[1] The *Corporate Income Tax and Franchise Act* defines unitary corporations as "two or more integrated corporations … that are owned in the amount of more than fifty percent and controlled by the same person and for which at least one of the following conditions exists:

(1) there is a unity of operations evidenced by central purchasing, advertising, accounting or other centralized services;
(2) there is a centralized management or executive force and centralized system of operation; or
(3) the operations of the corporations are dependent upon or contribute property or services to one another individually or as a group.

The Legislative Finance Committee (LFC) Fiscal Impact Report (FIR) on SB 389 refines the TRD estimates based on the fact that the distribution to the Public School Fund will be made from net receipts. Noting that the TRD estimates are based on before-credit (gross) receipts, the LFC staff estimates that the distributions to the fund would be $81.1 million in FY 10; $59.9 million in FY 11; $64.6 million in FY 12; and $70.9 million in FY 13.

Although SB 389 does not contain any contingency language, a House Appropriations and Finance Committee (HAFC) amendment to HB 331, *Public School Funding Formula*, made implementation of the proposed funding formula contingent upon the enactment of HB 346 (now CS/HB 346), SB 389, or SB 412 and on the generation of at least $350.0 million in additional state revenue for FY 11.

In January 2009, American Institutes for Research (AIR), the contractor for the funding formula study, provided an updated estimate of the additional cost of funding marginal sufficiency[2] and the first year of the three-year hold harmless provision for school districts and charter schools that may see their program cost reduced. This estimated additional cost is $345.3 million.

Issues:

TRD notes that all other Western states with a corporate income tax currently mandate combined reporting, and that, in 2003, the Governor's Blue Ribbon Tax Commission endorsed the concept of mandatory combined reporting.

During the 2008 interim, all 89 school districts were invited to work with the Legislative Education Study Committee to examine the potential impact on school district programs and student achievement of the public school funding formula initially proposed during the 2008 legislative session. Part of that discussion centered around potential revenue sources for the additional revenue needed to implement the proposed formula. Most school districts stated that their communities would support an increase in the Gross Receipts Tax if there were assurances that the revenue would be used exclusively to support the sufficiency funding needed to implement the proposed funding formula.

Technical Issues:

TRD points out that the January 1, 2009 implementation date means that some corporations will have to change the way in which they calculate taxes in the middle of a taxable year:

> There is no effective date prescribed for distributions to the Public School Fund to begin. Making the changes applicable to tax years beginning on or after January 1, 2009 would change the tax reporting method required from many corporations for their current tax year, which is already underway. These corporations would be required to change their tax computations almost immediately in order to make estimated payments by June 15, 2009. TRD would not be able to provide much guidance to affected companies; significant lead time would be required to develop regulations and other guidance. A delayed applicability date would allow corporations time to implement the change and TRD time to provide crucial guidance.

[2] Marginal sufficiency is the difference between the projected statewide cost of providing a sufficient education as determined by the funding formula study and the current statewide program cost.

<u>Related Bills</u>:

HB 331a *Public School Funding Formula*
CS/HB 346 *Education Gross Receipts Surtax* (0.75%)
SB 412 *Education Gross Receipts Surtax* (0.75%)
SB 648 *Corporate Income Tax Rates & Payments*