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FISCAL IMPACT REPORT

ORIGINAL DATE 01/25/10

SPONSOR Feldman & Picraux LAST UPDATED _____ HB _____

SHORT TITLE No Soft Drink Gross Receipts Deduction SB 31

ANALYST Gutierrez

REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Non-Rec	Fund Affected
FY10	FY11	FY12		
	\$8,925.0	\$9,355.0	Recurring	County-supported Medicaid fund
	\$3,649.0	\$3,825.0	Recurring	General Fund

(Parenthesis () Indicate Revenue Decreases)

Relates to SB10 and SB81

SOURCES OF INFORMATION

LFC Files

Responses Received From

Taxation and Revenue Department (TRD)
 Department of Health (DOH)
 New Mexico Health Policy Commission (HPC)

SUMMARY

Synopsis of Bill

Senate Bill 31 amends Section 7-9-92 NMSA 1978 to remove “soft drinks” from the list of foods eligible to receive a gross receipts tax deduction for retail food that was enacted in 2004. Soft drinks are defined as nonalcoholic flavored beverages commonly referred to as soft drinks that contain a sweetener additive or are made from powder, syrup, concentrate or any other base product.

The effective date of this provision will be July 1, 2010.

FISCAL IMPLICATIONS

According to the U.S. Census Bureau’s 2008 Consumer Expenditure Survey, households in the Western Region spend roughly \$379 on “nonalcoholic beverages” a year for their at home

consumption. According to the 2009 Beverage World State of the Industry report, roughly 66 percent of all nonalcoholic beverages are “soft drinks”. It is assumed for this estimate that there are 746,365 households in NM in FY10, thus there are \$283 million nonalcoholic beverage expenditures in NM in FY10. These nonalcoholic beverage expenditures are grown at the same rate as food deductions for future years (using Global Insights consumer price index for food). Using Beverage World’s estimate of 66 percent for soft drinks, there are \$178.5 million soft drink receipts excluded from the gross receipts tax food deduction (assuming 90 percent of all soft drink purchases currently qualify for the food deduction) in FY11.

This bill distributes \$8.9 million, the State’s 5 percent gross receipts tax (GRT), to the county-supported Medicaid fund in FY11. Because the soft drinks are no longer part of the gross receipts food deduction, the general fund no longer has to make hold harmless distributions for soft drink sales and the general fund now receives the revenue from its part of the State’s 5 percent tax which is 3.775 percent. These two pieces generate \$12.6 million for the general fund but the general fund must then distribute the \$8.9 million to the county-supported Medicaid fund, thus leaving the general fund with a revenue increase of \$3.6 million in FY11. Local governments will collect their local option taxes including the municipalities 1.225 percent of the State GRT, thus offsetting the loss of “hold harmless” distributions they will no longer receive on soft drink deductions.

SIGNIFICANT ISSUES

The bill may discourage consumption of soft drinks by increasing their price relative to other beverages.

By broadening the gross receipts tax base slightly, the bill would allow a lower tax rate to generate the same amount of revenue.

TRD:

Currently, gross receipts tax does apply to sales of soft drinks at restaurants, bars, vending machines, movies, sporting events or other concession locations, and any retail location that does not qualify for the food deduction. Because of federal preemption, soft drinks would still be exempt from the gross receipts tax when purchased with food stamps. There will be a high initial and moderate continuing compliance cost to taxpayers. There are no taxpayer penalties for not reporting or misreporting their soft drink sales; therefore, based on past experience, proper reporting compliance is expected to be low.

ADMINISTRATIVE IMPLICATIONS

TRD:

This bill will have a high overall impact on the Department. It will necessitate high taxpayer education with little time to distribute and insure comprehension of all required information. The sales would need to be separately reported and identified on the CRS-1 Form, using either a new special rate code or a new location code, so that proper distributions could be made. More lines of detail would result in lengthier returns, thus affecting processing of CRS forms for the retail stores, as more of the full-page CRS-1 long forms are filed. This proposal would place an additional burden on the Audit and Compliance Division to

examine, in more detail, the deductible sales, to ensure that the gross receipts tax on soft drinks was paid. Instructions and publications will need revision at minimal costs.

In addition, four years of experience with the current (simpler) food deduction indicates that a high number of errors would occur in reporting, which would adversely affect “hold harmless” distributions to local governments and the new distribution to the CSMF. These taxpayer reporting errors would often require significant resources to research, correct, and explain to local officials and other distribution recipients.

Creating the ability to make a new distribution based on the amount of the gross receipts tax revenue from soft drinks at a retail food stores will have a moderate IT impact broken down as follows:

- 1) Changes to the pipeline for E-DCR - 60 hours
 - 2) Changes to configuration for the new rate type – 160 hours
 - 3) Changes to revenue accounting – 160 hours
 - 4) Changes to TAP and NMWebFile – 160 hours
 - 5) Testing – 40 hours
- Total IT impact 580 hours

RELATIONSHIP

This bill relates to:

- SB10 which amends the gross receipts food deduction by changing the definition of food to staple foods as defined by the federal supplemental nutrition assistance program (SNAP).
- SB81 which expands the definition of retail food store to include those establishments which have more than 75 percent of the total sales consisting of bottled water, ice and coffee.

TECHNICAL ISSUES

Page 2, lines 4, 16, and 17 refer to the “federal food stamp program” and should reflect the program’s change of name to the “federal supplemental nutrition assistance program”.

TRD:

Because a beverage “commonly referred to as a soft drink” is ambiguous, the proposal would make the food deduction very difficult to interpret. For example, a store might sell Coca-Cola, Red Bull and fructose-sweetened green tea. Under the proposal Coca-Cola would not be eligible for the food deduction; however, it is unclear what the approach would be with the other two products. Red Bull, for example, is marketed as an “energy drink” and is sweetened with glucose rather than the more common sucrose, or fructose. It is unclear if Red Bull would remain eligible for the food deduction by virtue of its use of glucose, or by virtue of its marketing campaign as an “energy drink.” Additionally it would be unclear if fructose-sweetened green tea would remain deductible.

The Streamlined Sales Tax Agreement allows certain deviations from the basic definition of food, such as excluding soft drinks; however, it does not allow the definition of soft drinks used in this bill¹. If adopted, therefore, New Mexico would not qualify for Streamlined without repealing the changes in the bill.

OTHER SUBSTANTIVE ISSUES

DOH:

Sweetened beverage consumption has doubled in adults and tripled in adolescents in the US since the 1970s. During the same time period, milk consumption decreased by 30% (USDA Economic Research Service, 2002). Recently published studies in leading medical journals suggest a link between dairy consumption and lower body weight among adults and youth. As non-nutritive sweetened drink consumption in youth rises, including drinks sweetened with the sugar substitute aspartame, milk consumption declines. As the American Academy of Pediatrics notes, milk is the primary source of calcium in the diets of children and adolescents.

BLG/svb

The Legislative Finance Committee has adopted the following principles to guide responsible and effective tax policy decisions:

- 1. Adequacy:*** revenue should be adequate to fund government services.
- 2. Efficiency:*** tax base should be as broad as possible to minimize rates and the structure should minimize economic distortion and avoid excessive reliance on any single tax.
- 3. Equity:*** taxes should be fairly applied across similarly situated taxpayers and across taxpayers with different income levels.
- 4. Simplicity:*** taxes should be as simple as possible to encourage compliance and minimize administrative and audit costs.
- 5. Accountability/Transparency:*** Deductions, credits and exemptions should be easy to monitor and evaluate and be subject to periodic review.

More information about the LFC tax policy principles will soon be available on the LFC website at www.nmlegis.gov/lcs/lfc

¹ Under definitions of the Streamlined Sales and Use Tax Agreement, Adopted November 12, 2002 and amended through September 30, 2009:

“**Soft drinks**” means non-alcoholic beverages that contain natural or artificial sweeteners. “Soft drinks” do not include beverages that contain milk or milk products, soy, rice or similar milk substitutes, or greater than fifty percent of vegetable or fruit juice by volume.