F I S C A L   I M P A C T   R E P O R T

SPONSOR Griego, E. **ORIGINAL DATE** 02/03/10 **LAST UPDATED** **HB**

SHORT TITLE Create Tax Expenditure Study Commission **SB** 50

ANALYST Lucero

APPROPRIATION (dollars in thousands)

Appropriation		Recurring or Non-Rec	Fund Affected
FY10	FY11		
$200.0		Nonrecurring	General Fund

(Parenthesis ( ) Indicate Expenditure Decreases)

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY10	FY11	FY12	3 Year Total Cost	Recurring or Non-Rec	Fund Affected
Total		$150.0		$150.0	Nonrecurring	General Fund

(Parenthesis ( ) Indicate Expenditure Decreases)

SOURCES OF INFORMATION
LFC Files

Responses Received From
Taxation and Revenue Department (TRD)

SUMMARY

Synopsis of Bill

Senate Bill 50 appropriates two hundred thousand dollars ($200,000) from the general fund to the Legislative Council Service for staff salaries, contracted staff, and reimbursement of per diem and mileage expenses associated with the proposed tax expenditure study commission created by the bill.

The seventeen member commission would include three members appointed by the speaker of the House of Representatives, three members appointed by the Senate Pro Tempore, and eleven members appointed by the governor including one member to represent municipal government and one to represent county government. The governor, in consultation with the Speaker and Pro Tempore, shall appoint the chair of the commission from among the members of the commission.

The Commission would be required to prepare a report of its findings on the cost and benefit of each tax expenditures authorized by New Mexico law in effect during calendar years 2009 and 2010, and submit the report, including specific recommendations and proposed legislation to the governor and the Legislative Council Service no later than July 1, 2011.

The report would list;

- The total amount of each tax expenditure "or public revenue foregone or the current value or approximate value of each tax benefit received by taxpayers in each calendar year;"
- The aggregate number of taxpayers benefiting from the expenditures, and where practical and permitted by law, the amounts or values of the benefit to each taxpayer;
- The location of taxpayers and benefit amounts and values aggregated by municipality and county;
- The number of new jobs created or new employees hired by each taxpayer as a result of each tax expenditure. For each "new job" the report would include the employee's wage, gender and state of residence immediately prior to employment; and
- Any other information the commission may deem useful to understand a tax expenditure.

The bill defines "tax expenditure" as "a tax deduction, an exemption, a rebate, a credit or exclusion or a preferential tax rate or other special tax treatment." "Taxpayer" is defined as an individual, corporation, business entity, or other person eligible to receive or has received a tax expenditure.

FISCAL IMPLICATIONS

The appropriation of two hundred thousand dollars ($200,000) contained in this bill is a nonrecurring expense to the general fund and may be expended in fiscal years 2010 and 2011. Any unexpended or unencumbered balance remaining at the end of fiscal year 2011 shall revert to the general fund.

SIGNIFICANT ISSUES

Tax expenditures give preferential tax treatment to a specific group to encourage certain types of economic activity. From a tax policy standpoint, these mechanisms by which the revenue base is eroded should be evaluated as rigorously as appropriations.

Uncovering the degree of erosion in a state's tax base is important for several reasons. Without knowing the amount of revenue forgone due to tax expenditures, policymakers and the public cannot know how much tax relief is being granted and to whom the benefits are accruing. Also, a narrower tax base requires that a higher tax rate be charged on everything that remains taxable to provide enough revenue to meet the state's spending needs. Finally, a narrower tax base leads to increased revenue volatility, which makes fiscal planning more difficult.

Currently, the cost of New Mexico's tax expenditures are only estimated when they are first enacted in Fiscal Impact Reports (FIR). However, the costs of tax expenditures are rarely revisited to assess whether they cost more or less than expected, whether costs are growing as anticipated, or whether tax expenditures are effective. Additionally, FIRs tend to only quantify the direct effects of tax expenditures and do not attempt to include dynamic revenue effects such as job creation or increased economic activity. For this reason, tax expenditure estimates may overstate the true costs of some successful tax incentives.

According to the Taxation and Revenue Department (TRD):

- Information on tax expenditures by the location of taxpayers and the benefit amounts and values aggregated by municipality and county could result in identification of a taxpayer qualifying for the benefit, which would violate tax confidentiality statutes (Sections 7-1-8 through 7-1-8.10 NMSA 1978).

- Tax forms do not generally require the taxpayer to disclose much of information identified in the bill including the municipality and county where credits are earned or used, the number of jobs created or employees hired, wage or salary information, gender, the state of residence immediately prior to employment, and other tax preferences. Compiling the data may require independent solicitation of information from taxpayers.

- Due to the sizable number of tax expenditures, the approximate one-year period proposed in which the Commission is to perform its duties will be may be too short to identify, gather required data on, and analyze all tax expenditures.

- In addition to tax expenditures, the Commission report is to include the amount of any "public revenue foregone or the current value or other approximate value of each tax benefit received by taxpayers in each calendar year". Both the meaning and the intended scope of this language is unclear.

- The definition of "tax expenditures" would apparently include deductions, etc. in the federal Internal Revenue Code that flow through to New Mexico taxes through our adoption of federal tax bases (primarily for the personal and corporate income taxes). For nearly all of these federal flow-through tax expenditures, there is no information on state tax returns and little or no information from available federal tax returns that would be required in order for the Commission to estimate the amount of such tax expenditures. It is also unclear how useful this information would be to the Governor or the Legislature, since the State cannot amend the Internal Revenue Code.

- At a minimum, the per diem expenses of 17 members to meet the minimum two meetings per month would require about $65 thousand of the $200 thousand appropriation. Presumably, charged with such an enormous task, the Commission may see the need to meet even more frequently. There may be relatively little money available from the appropriation to hire any professional staff for research and data gathering.

PERFORMANCE IMPLICATIONS

Periodic review of tax expenditures adds transparency, fiscal discipline, and political accountability to the budget process. By uncovering the cost of New Mexico's tax expenditures, the state's policymakers may be better equipped to tailor tax incentives and appropriations to better achieve the state's goals.

ADMINISTRATIVE IMPLICATIONS

The bill states that the Commission "may request assistance from the Legislative Council Service, the Taxation and Revenue Department and the Economic Development Department." TRD notes that since large amounts of data would be required from the department, it seems likely that the proposed bill would require extensive use of the Department's resources.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

Relates to HB82 "Develop Tax Expenditure Budget"

TECHNICAL ISSUES

The bill is silent on how an agency that is bound by confidentiality or other non-disclosure statutes is supposed to reconcile those restrictions with the demands of this section.

OTHER SUBSTANTIVE ISSUES

Like most states, New Mexico's tax code contains hundreds of tax expenditures. The gross receipts and compensating tax code (Chapter 7, Article 9 NMSA 1978) includes about 100 exemptions, deductions, and credits. The personal and corporate income tax codes (Chapter 7, Articles 2 and 2A NMSA 1978) also include dozens of tax expenditures. While many of New Mexico's tax expenditures have very small costs, they cumulatively represent a significant erosion of the state's revenue base.

TRD notes that without any statutory mandate, the department has undertaken a multi-year, comprehensive review and analysis of tax expenditures. The first report prepared as part of this effort has been completed and released. The second report is near completion. The department also recently released detailed information on tax expenditures in the form of business incentive credits in a joint report with the Economic Development Department to the Legislative Finance Committee and the interim Revenue Stabilization and Tax Policy Committee. The department believes that this comprehensive, multi-year plan will allow the department to provide the Governor and the Legislature a carefully prepared and highly useful series of reports that will help inform policy debates and policy decisions well into the future.

TRD's multi-year, comprehensive review and analysis of tax expenditure report includes an in depth description of the concept and framework for analysis of tax expenditures, major taxes, including the gross receipts and compensating taxes; the gasoline, alcohol, cigarette and motor vehicle excises, the personal and corporate income taxes, taxes related to severance of oil, gas, coal, uranium, and minerals; the insurance premiums tax; gaming taxes; and the property tax. In addition, the department reports on manufacturing tax incentives. The reports were reported to legislative committees most recently during the 2009 interim.

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