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

ORIGINAL DATE 02/10/10
SPONSOR Jennings **LAST UPDATED** **HB**

SHORT TITLE Nonprofit Entity Gross Receipts **SB** 261

ANALYST Gutierrez

REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Non-Rec	Fund Affected
FY10	**FY11**	**FY12**		
	$8,000.0 - $11,000.0	$9,000.0 - $12,000.0	Recurring	Counties
	$35,000.0 - $47,000.0	$37,000.0 - $50,000.0	Recurring	Municipalities
	$26,000.0 - $35,000.0	$20,000.0 - $28,000.0	Recurring	General Fund

(Parenthesis ( ) Indicate Revenue Decreases)

Relates to SB271

SOURCES OF INFORMATION
LFC Files

Responses Received From
Taxation and Revenue Department (TRD)

SUMMARY

Synopsis of Bill

Senate Bill 261 modifies the gross receipts tax exemption for nonprofit organizations that are 501 (c)(3) or 501(c)(6) classified. This bill requires these organizations to demonstrate to the department that the organization's receipts from commercial activity in the prior twelve months did not exceed $10 million. If their receipts did exceed $10 million, then all their receipts for commercial activity (does not include donations, dues or registration fees) would be subject to the gross receipts tax.

The effective date of this bill's provisions is July 1, 2010.

FISCAL IMPLICATIONS

The fiscal impact is intended to give you a flavor of the impact but allows for a range due to the large amount of assumptions that had to be made.

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

TRD:

The basic data used for this estimate is Form 990 from the U.S. Internal Revenue Service (IRS). This form gives information on income and assets of all 501(c) organizations.

The 501(c)'s were grouped into hospital and non-hospital 501(c)3s, 501(c)3 foundations, and 501(c)(6)s for separate treatment in the calculations. The majority of foundation income was assumed to come from donations or investment income which would remain exempt from the gross receipts tax. Also a quarter of regular 501(c)(3) income and two-thirds of 501(c)(6) income was assumed to remain exempt because it comes from donations or dues and registration fees. Roughly half of all non-exempt income from these organizations was assumed to be deductible under existing gross receipts tax deductions, which is comparable to the portion of other service sector entities.

Hospitals must be separated out because they account for almost 40% of all 501(c)(3) income and would qualify for the Hospital Gross Receipts Tax Credit once they become taxable. This credit is in the process of phasing in and by FY12 it will remove the portion of their gross receipts tax liability that is distributed to the State. In FY11 it removes 80% of this liability.

The IRS data contains the main address of each organization; however, there is no data to apportion the organization's income between States. It was assumed that all income from entities with New Mexico addresses was from inside New Mexico. The total income for non-hospital entities in New Mexico was increased to account for non-New Mexico headquartered organizations. For example there is a separate unit of Goodwill for New Mexico but not for the Salvation Army.

From the data available it is not clear which entities may be considered related entities for purposes of exceeding the $10 million threshold and it is also not clear how many entities could restructure and become sufficiently unrelated entities in order to avoid exceeding the $10 million threshold.

SIGNIFICANT ISSUES

TRD:

Exempting non-profit receipts from taxation is a tax expenditure. However, nonprofits are generally involved in activities that are similar to, or direct alternatives to, activities by governments. Removing tax exemption could therefore require additional spending by government or forgoing the benefits of the activities currently conducted by nonprofits.

ADMINISTRATIVE IMPLICATIONS

TRD:

Examining applications from non-profits attempting to demonstrate their receipts from commercial activity in the prior twelve months were below $10 million will create a significant new function for the Audit and Compliance Division; if done thoroughly it may be comparable to a full-scope audit. Auditing taxpayers would also be difficult and self-compliance is expected to be low.

CONFLICT

This bill conflicts with SB271 which repeals the section to which SB261 is amending.

TECHNICAL ISSUES

TRD:

The language in the bill that refers to the "prior twelve months" in relation to the $10 million threshold should be clarified to specify either the previous calendar year or the previous fiscal year. Without this clarification the "prior twelve month" period would be moving, making compliance and administration of this section difficult.

OTHER SUBSTANTIVE ISSUES

To the extent that non-profits are engaged in the same kinds of commercial activities as for-profit organizations, this proposal could be seen as "leveling the playing field". This improves equity and efficiency.

TRD:

It may be difficult for a group of new taxpayers to register, become familiar with, and begin paying the gross receipts tax by August 25, 2010 (1st filing deadline after effective date). This bill will place a compliance cost on all exempt non-profits by forcing them to demonstrate their commercial activity receipts were below $10 million. There would be an incentive to restructure into small entities.

BLG/mt

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