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

ORIGINAL DATE 02/04/11
SPONSOR Smith **LAST UPDATED** **HB**

SHORT TITLE Tax Forms Itemizing Gross Receipts Exemptions **SB** 170

ANALYST Graeser

REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Non-Rec	Fund Affected
FY11	**FY12**	**FY13**		
	NFI	NFI	Recurring	General Fund
	NFI	NFI	Recurring	Local Funds

(Parenthesis ( ) Indicate Revenue Decreases)

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY11	FY12	FY13	3 Year Total Cost	Recurring or Non-Rec	Fund Affected
Total	$872.0	$470.0	$470.0	$1,812.0	Recurring	Taxation and Revenue Dept. Operating Funds (General Fund)

(Parenthesis ( ) Indicate Expenditure Decreases)

Note: this estimate does not income the cost of reporting deductions allowed under the Gasoline Tax Act.

SOURCES OF INFORMATION
LFC Files

Responses Not Received From
Taxation and Revenue Department (TRD)

SUMMARY

Synopsis of Bill

Senate Bill 170 would require taxpayers to itemize and report details of tax credits, exemptions and deductions claimed pursuant to the Gross Receipts and Compensating Tax Act, The Interstate Telecommunications GRT and the Gasoline Tax Act. Taxpayers would be required to report on over 100 gross receipts and compensating tax exemptions and deductions, identifying and separately stating each on a form provided by the Taxation and Revenue Department. The proposal makes an exception for taxpayers who are reporting any of 16 specific exemptions allowed in the Gross Receipts and Compensating Tax Act if the sole purpose of their reporting would be to claim these exemptions. The bill also requires citizens who claim exemption from the Income Tax Act to file a tax return stating income from any business transaction, property or employment in New Mexico and identifying the exemption to which the person is entitled. The bill does not require detailed reporting of exemptions, deductions and credits granted pursuant to the Corporate Income Tax Act (7-2A-1 through 26 NMSA 1978).

Effective Date: January 1, 2012; applicable for reporting exemptions allowed pursuant to the Income Tax Act (Section 2 of the bill; 7-2-12 NMSA 1978 TAXPAYER RETURNS of the Income Tax Act.)

FISCAL IMPLICATIONS

This bill has no significant revenue impact. The purpose of the extensive reporting is to assist the Department in preparing comprehensive tax expenditure reports as required by HB 161 and SB 47.

The operating budget impact, however, is substantial. The bulk of the administrative burden will be processing the forms needed to report deductions, exemptions and credits allowed under the Gross Receipts and Compensating Tax Act. TRD reports in the analysis of SB 39 that, "…to eliminate the delays expected in processing paper returns, the Revenue Processing Division would need the following:

1) One new full page scanner at $340,000 would be required to process the expanded forms. Cost would also include $160,000 annually for the maintenance contract.
2) Nine additional FTE at a cost of $300,000: for five processors, two data entry and two edit error employees.
3) Increased e-file requirements and compliance will eventually reduce some costs of the proposal but time and money will be needed initially to educate and support taxpayers resistant to electronic filing and to ensure smooth implementation."

This level of equipment support will probably handle the reporting required for Gasoline Tax and Interstate Telecommunications GRT. It may not be necessary to add equipment to process the details required for Income Tax Act exemptions, but there will be some form design changes that will have to be made during the regular, annual forms design effort.

This proposal will have a moderate impact on the Department's Information Technology Division. In its analysis of SB-39, TRD reports this cost for the Gross Receipts and Compensating Tax reporting of approximately $72,000 using 800 employee hours. Adding reports pursuant to the Interstate Telecommunications GRT (Reported on the CRS-1) will probably take no additional time. IT changes for Gasoline Tax will add to the time and resources required to implement the new report, however, TRD would have to estimate these additional, marginal costs over the levels reported in SB-39. Changes to report exempt income under the Income Tax Act would be accomplished in the regular, annual maintenance effort. Resources required to make application changes, system updates and configuration changes are extensive. Multiple developers would be assigned to handle the front-end applications, the data entry application and the processing application. Structure changes and the extract code would add additional hours. Unlike SB-39 which has an effective date of July 1, 2011, this bill's effective date is January 1, 2012, allowing the Department to deliver the IT portion of the implementation with current staffing resources.

SIGNIFICANT ISSUES

TRD identifies a number of significant issues:

1. This proposal would increase the cost of doing business in New Mexico. Many people and businesses who do not currently file CRS-1 Forms will be required to register and begin reporting. Taxpayers who are already reporting will have a greatly increased reporting burden for Gross Receipts and Compensating Taxes, Interstate Telecommunications GRT and Gasoline Taxes. New Mexico will change from a state with one of the easiest reporting requirements for the general sales tax to one of the most burdensome.
2. The bill will generate more data on the cost of New Mexico's gross receipts tax (GRT) and compensation tax exemptions and deductions; however, not all of those exemptions and deductions are tax expenditures and the quality of that data will be questionable.
3. The quality and accuracy of the data obtained by the new reporting requirements will be questionable. Because there are no penalties associated with the new reporting requirements it is likely that taxpayers will not comply fully or correctly. As long as the correct liability is reported and paid, the Department does not have any compliance tools to encourage taxpayers to fully itemize their exemptions and deductions. Based on experience with food and medical deductions and gasoline location reporting, there will be many problems with correct reporting even after significant taxpayer outreach and education.
4. Only taxpayers with receipts entirely attributable to the following exemptions would not be required to register and begin reporting to the Department:
   - Section 7-9-13(A): GRT exemption for certain sales by governmental agencies
   - Section 7-9-13.1: GRT exemption for services performed outside the state the product of which is initially used in New Mexico
   - Section 7-9-13.4: GRT exemption for sale of textbooks from certain bookstores to enrolled students
   - Section 7-9-13.5: GRT and governmental gross receipts tax exemption for event center surcharges
   - Section 7-9-14: GRT exemption for governmental agencies
   - Section 7-9-17: GRT exemption for wages
   - Section 7-9-18.1: GRT exemption for food stamps
   - Section 7-9-22: GRT exemption for vehicles
   - Section 7-9-22.1: GRT exemption for boats
   - Section 7-9-23: compensating tax exemption for vehicles
   - Section 7-9-23.1: compensating tax exemption for boats
   - Section 7-9-25: GRT exemption for dividends and interest
   - Section 7-9-26: GRT exemption for fuel
   - Section 7-9-28: GRT exemption for occasional sale property or services
   - Section 7-9-41.3: GRT exemption for sales by disabled street vendors

PERFORMANCE IMPLICATIONS

Because of the large scope of this requirement, other core tasks of the Department might get less attention than otherwise.

ADMINISTRATIVE IMPLICATIONS

TRD reports that this bill would create severe administrative costs on the Department and the compliance costs on taxpayers. The following statement is copied from the analysis for SB-39, which has a July 1, 2011 effective date. This bill extends that effective date to January 1, 2012.

"The administrative impact to the Department would be large. The Department would not be able to correctly or effectively implement the proposed requirements by July 1, 2011, even with a significant increase in resources. A more realistic implementation date would be July 1, 2012. The Department would need to significantly revise and expand the CRS-1 Form in order for over 100 exemptions and deductions to be separately reported and captured. Taxpayer education would require numerous workshops throughout the state, including the rural communities where many agricultural businesses would now be required to report. Education of the Department employees would take time. With current processing equipment and resources there would be a drastic increase in processing time and a corresponding delay in making distributions to local governments. The current half-page CRS-1 Form would become a full page or multiple page form for many taxpayers. Processing multiple pages will significantly increase the cost and time need. Taxpayers reporting requirements will increase for all taxpayers, even the ones that file electronically. Not only the size of returns but also the number of returns will increase substantially."

Similar comments might apply to the Gasoline Tax changes.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

SB-170 Relates to HB 161, TAX EXPENDITURE BUDGET DEVELOPMENT AND REPORT and SB 47, TAX EXPENDITURE BUDGET DEVELOPMENT AND REPORT

SB 170 is similar to SB 39 TAX FORMS ITEMIZING GROSS RECEIPTS EXEMPTIONS, however, SB 39 only requires reporting detailed information on gross receipts tax credits, exemptions and deductions, whereas this bill requires reporting details for Gross Receipts and Compensating Tax, Interstate Telecommunications GRT and the Gasoline Tax Act and requires additional taxpayers to report income exempt from the Income Tax Act.

TECHNICAL ISSUES

The bill's reporting exception is only applied to the <u>person</u> whose receipts are comprised entirely of the 16 specific reporting exceptions and not those exemptions themselves. For example a person with any taxable receipts would still be required to report and itemize receipts from their wages and any occasional sale of property or services (such as a garage sale).

ALTERNATIVES

Perhaps an alternative to this complex, monthly credit, exemption and deduction reporting requirement with doubtful accuracy would be a stand-alone annual reconciliation report that would have to be filed by any person using a credit, exemption or deduction in the course of the year. The legislature could impose a failure to file penalty proportional to the amount of the credit, exemption or deduction not reported. This standalone report would be roughly $1/5^{th}$ as costly to process as a series of monthly, quarterly or semi-annual detailed reports.

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL

In the absence of this bill, the Department will have difficulty assessing the impact of various tax expenditures. Even with this bill, the task of accurately determining the fiscal impact of various tax expenditures is still not trivial. Both of the tax expenditure reporting bills in this session (SB-47 and HB-161) require an estimate of offsetting positive impacts, such as the number of jobs created or saved by the tax expenditure. The reporting requirement in either SB-39 or SB-170 will not assist the determination of these positive impacts.

LG/bym