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

ORIGINAL DATE 2/5/16
SPONSOR Smith **LAST UPDATED** **HB**

SHORT TITLE Delay Corprate Income Tax Reductions **SB** 252

ANALYST Graeser

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY16	**FY17**	**FY18**	**FY19**	**FY20**		
$4,700.0*	$23,700.0	$42,700.0	$37,700.0	$21,400.0	Recurring	General Fund

Parenthesis ( ) indicate revenue decreases

(*) Because of the "safe harbor" rules, the April and June 2016 estimated payments of TY 16 liability would be voluntary and not mandatory for many taxpayers. This number is less certain than the other items in the table.

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY16	FY17	FY18	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
Total	$0.0	$35.0	$0.0	$35.0	Nonrecurring	TRD operating

Parenthesis ( ) indicate expenditure decreases

Conflicts with SB 90 which proposes a one-year delay in the corporate income tax rate reduction phase-in, but does not adjust the sales-only factor phase-in.

SOURCES OF INFORMATION

LFC Files

Responses Received From
Taxation and Revenue Department (TRD)
Economic Development Department (EDD)

SUMMARY

Synopsis of Bill

Senate Bill 252 delays for two years the periods over which the corporate income tax cuts and single sales factor apportionment methodology of the 2013 tax bill are phased in. The rates are frozen at the TY 16 levels for two years.

There is no effective date of this bill. It is assumed that the new effective date is 90 days after this session ends (May 18, 2016). This bill contains an emergency clause, and would become effective immediately upon signature by the governor, provided that it passed both houses by 2/3rd majority.

FISCAL IMPLICATIONS

TRD estimated the fiscal impact of this bill:

> "SB 252 delays the implementation of the corporate income tax (CIT) reduction and the phase-in of the use of single sales factor in apportioning (SSF) in TY2017 and TY2018. Under existing law, the top CIT rate is reduced from 7.3% to 6.9% in TY15 and from 6.9% to 6.6% in TY16 (see first chart in Methodology for Estimated Revenue Impact - Detailed Discussion). This bill proposes to delay the TY16 top CIT rate reduction to TY18 and all subsequent rate reductions by two years. This delay in rate reductions will impact three quarters of the estimated payments in TY16 and one-quarter of the estimated payment in FY16. The delay in the rate reduction will partially impact FY16, a full impact on FY17 through FY20, a partial impact in FY21, and no impact after that. To determine the fiscal impact on the General Fund, the Taxation and Revenue Department (TRD) analyzed the difference between the previously estimated impact (see second chart in Methodology for Estimated Revenue Impact - Detailed Discussion) of the rate reduction and the SSF and shifting those impacts by two years. These percentage changes were applied to the January 2016 consensus General Fund revenue estimate."

SIGNIFICANT ISSUES

TRD notes the following: "… by delaying the rate reduction and the SSF phase-in, the bill should increase revenue for five fiscal years because each of these fiscal years contains all or portions of tax years effected by the delayed reduction. However, CIT rates were reduced and the SSF was phased-in in order to keep New Mexico competitive with other states in terms of economic development. The impact of the delayed deduction, in terms of economic development is unknown."

Reiterating the last two sentences above, EDD has a major objection to this bill:

> "The bill will have a positive fiscal impact in the short term, as it will increase corporate income tax revenues by delaying the rate reductions and apportionment formula changes. It will have a significant negative impact over the longer term, however, more so even than not having enacted the changes in the first place. The 2013 tax package has had a huge impact on the state's competitiveness and ability to attract companies with the option to locate in multiple states. Each business that relocates to or expands in New Mexico increases revenues. The bill will destroy the state's ability to realize those revenues. Large businesses and site selectors consistently list governmental stability and predictability as a critical factor in choosing locations for new facilities. The 2013 changes to the corporate income tax structure are valuable to businesses in and of themselves, of course. But they also represent a business-friendly environment that appeals to businesses at a different level. The bill signals to businesses and site selectors that structural reforms to make the state competitive are worth no more than the paper they are printed on because they will be repealed at the first sign of economic distress. The businesses EDD and the Partnership are trying to attract to the state are considering

making multi-million dollar capital investments. They simply will not do so if they believe the incentives used to recruit them are subject to annual political whims. Thus the state will not only lose the CIT revenue from the later-implemented changes, but will fail to capture the increased revenues from relocating businesses. According to a November 2015 article on Georgia's competitiveness in Site Selection magazine,

> Sound fiscal health is a sign of strong leadership, particularly in challenging economic circumstances. Even more challenging is being able to offer — and then delivering on — what capital investors most require, which is predictability — the feeling that their long-term investment in a location is a wise investment today and will be so in the future."

ADMINISTRATIVE IMPLICATIONS

TRD reports that this bill will have minimal impact on administration, as no procedural changes are required for the reporting of collections of CIT. Changes would be required in programming, and to forms, instructions and publications, that are inevitable with changes to the current law. No impact to financial distribution business processes.

Moderate ITD Impact (500 hours) –This would require changes to CIT rate configurations; also changes needed for the GenTax and Taxpayer Access Point document rules.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

Conflicts with SB-90 which proposes a one-year delay in the corporate income tax rate reduction phase-in, but does not adjust the sales-only factor phase-in.

TECHNICAL ISSUES

TRD points out a technical issue in the delay caused by the rate delay for a tax year already in progress. Because taxpayers with net income over $1,000,000 are already contemplating the rate of 6.6%, reduced from 6.9% in effect since January 1, 2016 under the current law, compliance issues arise and estimated payments may be lower than they should be. This causes concern that a taxpayer may be subject to an inappropriate penalty. While the "safe harbor" rules may apply for many taxpayers to avoid any estimated tax penalties, other taxpayers – particularly those who have declining base profits for TY 17 over TY 16, could find that all four of their estimated tax payments are short compared to the requirement. It might be useful to allow TRD to regulate this situation in the case of freezing provisions of the 2013 law. Because this is a temporary delay, granting a temporary relief from estimated tax penalties for CIT taxpayers would be equitable.

Does the bill meet the Legislative Finance Committee tax policy principles?

1. **Adequacy**: Revenue should be adequate to fund needed government services.
2. **Efficiency**: Tax base should be as broad as possible and avoid excess reliance on one tax.
3. **Equity**: Different taxpayers should be treated fairly.
4. **Simplicity**: Collection should be simple and easily understood.
5. **Accountability**: Preferences should be easy to monitor and evaluate

<table>
<tr><th colspan="7">CHART 1: Current Law Rate Reductions</th></tr>
<tr><th></th><th>TY2013</th><th>TY2014</th><th>TY2015</th><th>TY2016</th><th>TY2017</th><th>TY2018</th></tr>
<tr><td>Income < $500k</td><td colspan="6">4.8%</td></tr>
<tr><td>Income $500k - $1m</td><td colspan="4">6.4%</td><td rowspan="2">6.2%</td><td rowspan="2">5.9%</td></tr>
<tr><td>Income > $1m</td><td>7.6%</td><td>7.3%</td><td>6.9%</td><td>6.6%</td></tr>
</table>

<table>
<tr><th>Tax Year</th><th>Apportionment Formula</th></tr>
<tr><td rowspan="2">2014*
(50%)</td><td>(2Xsales factor)+(property factor)+(payroll factor)</td></tr>
<tr><td>4</td></tr>
<tr><td rowspan="2">2015
(60%)</td><td>(3Xsales factor)+(property factor)+(payroll factor)</td></tr>
<tr><td>5</td></tr>
<tr><td rowspan="2">2016
(70%)</td><td>(7Xsales factor)+(1.5Xproperty factor)+(1.5Xpayroll factor)</td></tr>
<tr><td>10</td></tr>
<tr><td rowspan="2">2017
(80%)</td><td>(8Xsales factor)+(property factor)+(payroll factor)</td></tr>
<tr><td>10</td></tr>
<tr><td rowspan="2">2018
(100%)</td><td>(total sales in New Mexico)</td></tr>
<tr><td>(total corporate sales)</td></tr>
</table>

* 2014 is the same option in the old law

<table>
<tr><th colspan="8">CHART 2: Fiscal Impact of Rate Reduction and SSF Reduction</th></tr>
<tr><th colspan="8">Updated Impact Analysis Presented to RSTP in September 2015</th></tr>
<tr><th>Percentage impact of rate reduction</th><th>FY14</th><th>FY15</th><th>FY16</th><th>FY17</th><th>FY18</th><th>FY19</th><th>FY20</th></tr>
<tr><td>Current law impact</td><td>-3%</td><td>-12%</td><td>-19%</td><td>-26%</td><td>-31%</td><td>-38%</td><td>-38%</td></tr>
<tr><td>Proposed law impact</td><td>-3%</td><td>-12%</td><td>-19%</td><td>-19%</td><td>-19%</td><td>-26%</td><td>-31%</td></tr>
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