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

ORIGINAL DATE 2/28/2019
SPONSOR Munoz **LAST UPDATED** ______ **HB** ______

SHORT TITLE GRT Deduction For In State Freight Transport **SB** 347

ANALYST Graeser

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY19	FY20	FY21	FY22	FY23		
	Indeterminate; could be as much as ($2,000.0)				Recurring	General Fund
	Indeterminate; could be as much as ($600.0)				Recurring	Local Governments (as listed in fiscal impact section)

Parenthesis ( ) indicate revenue decreases

SOURCES OF INFORMATION
LFC Files

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

SUMMARY

Synopsis of Bill

Senate Bill 347 creates a new section of the Gross Receipts and Compensating Tax Act to allow a deduction for the receipts of a company transporting freight within the state if the company's principal place of business is located in New Mexico within thirty-five miles of an international port of entry on New Mexico's border with Mexico. The Taxpayer taking the deduction shall report it separately. Taxation and Revenue Department (TRD) shall compile an annual report on the deduction that shall include the number of taxpayers approved, the total amount approved, and other information necessary to evaluate the effectiveness of the deduction. TRD shall present the annual report to the revenue stabilization and tax policy committee and the legislative finance committee with an analysis of the effectiveness and cost of the deduction.

The effective date of this bill is July 1, 2019. There is no delayed repeal date but LFC recommends adding one.

FISCAL IMPLICATIONS

This bill narrows the gross receipts tax (GRT) base. See *Significant Issues* for more information.

According to the EDD analysis, "Communities of Columbus, Deming, Sunland Park, Anthony, Mesilla and southern Las Cruces are within the 35-mile zone as are unincorporated areas in Hidalgo, Luna, Dona Ana and Otero Counties." The specification is a business location within 35 miles of the port of entry. Only a very small portion of Otero County is within 35 miles of the Santa Teresa port of entry.

LFC staff present the following table extracted from TRD's RP500 for the entire Transportation and Warehousing NAICS code and for the entire counties of Dona Ana and Luna, as well as the municipalities of Deming, Anthony, Sunland Park. This is likely to result in an overestimate of fiscal impact, but is useful to determine an order of magnitude for a fiscal impact.

The fiscal impacts of the provisions of this bill are largely indeterminate for two reasons: (1) a substantial fraction of transportation charges would escape county and municipal gross receipts taxes pursuant to the provision 7-19D-5 NMSA 1978 (and 7-20E-5 for the county provision) which provides the only difference between the state definition of gross receipts and the definition for the purpose of the County or Municipal Local Option gross receipts taxes:

Sector 48-49 -- Transportation and Warehousing				
Activity Month	**Location**	**Total MTGR**	**Total Tax Paid**	**Total Recipient Paid**
FY16	Anthony, City of	711,490	55,793	19,187
FY17	Anthony, City of	538,687	42,390	20,130
FY18	Anthony, City of	766,381	60,103	21,914
FY16	Dona Ana County	24,071,298	1,834,536	315,547
FY17	Dona Ana County	24,181,785	1,880,460	333,098
FY18	Dona Ana County	29,003,157	2,264,309	416,742
FY16	Sunland Park	250,579	24,946	8,476
FY17	Sunland Park	192,414	17,104	10,162
FY18	Sunland Park	219,089	19,161	6,969
FY16	Deming	1,052,712	83,608	31,706
FY17	Deming	1,036,805	84,846	22,401
FY18	Deming	1,919,389	160,023	56,328
FY16	Luna County	10,940,912	765,909	182,144
FY17	Luna County	-5,891,818	-391,748	41,367
FY18	Luna County	3,278,923	252,582	40,614
FY16 Exposure		35,012,209	2,764,792	557,061
FY17 Exposure		18,289,967	1,633,052	427,159
FY18 Exposure		32,282,080	2,756,178	542,567

No tax authorized by the provisions of the Municipal Local Option Gross Receipts Taxes Act shall be imposed on the gross receipts arising from:

A. transporting persons or property for hire by railroad, motor vehicle, air transportation or any other means from one point within the municipality to another point outside the municipality; or

Although these sections relieve the transportation business of the local option gross receipts taxes for inter-jurisdictional transportation services, the state rate of 5.125% would apply.

The second reason for inability to establish a reasonable estimate is that TRD tracks business locations only to the county or municipality. Thus, if a transportation business were located in the northern portions of Las Cruces or Dona Ana County, it would not be eligible for the deduction, but TRD would have no way to ensure compliance with the provisions of this bill.

This bill creates or expands a tax expenditure with a cost that is difficult to determine but likely significant. LFC has serious concerns about the significant risk to state revenues from tax expenditures and the increase in revenue volatility from erosion of the revenue base. The committee recommends the bill adhere to the LFC tax expenditure policy principles for vetting, targeting, and reporting or be held for future consideration.

This bill may be counter to the LFC tax policy principle of adequacy, efficiency, and equity. Due to the increasing cost of tax expenditures, revenues may be insufficient to cover growing recurring appropriations.

SIGNIFICANT ISSUES

This bill narrows the gross receipts tax (GRT) base. Many of the efforts over the last few years to reform New Mexico's taxes focused on broadening the GRT base and lowering the rates. Narrowing the base leads to continually rising GRT rates, increasing volatility in the state's largest general fund revenue source. Higher rates compound tax pyramiding issues and force consumers and businesses to pay higher taxes on all other purchases without an exemption, deduction, or credit.

There are three ports of entry in New Mexico: Antelope Wells, Columbus and Santa Teresa. The Antelope Wells Port of Entry is remote and the nearest town – Janos, Chihuahua and Hachita are 45 miles from the port of entry. There is no significant revenue exposure from the provisions of this bill in Hidalgo County. Columbus port of entry is located 33 miles from the center of Deming in Luna County. So the provisions of this bill could be significant for Luna County and Deming. Columbus has no transportation activity reported on the RP500. The Santa Teresa port of entry is 45 miles from the center of Las Cruces. The provisions of this bill would apply primarily to transportation businesses in Anthony, Sunland Park, Santa Teresa and Deming.

United States Port of Entry	United States Road/Highway	City and State
Antelope Wells	NM 81	Antelope Wells, New Mexico
Columbus	NM 11(Ike Smalley Memorial Highway)	Columbus, New Mexico
Santa Teresa	NM 136 (Pete Domenici Boulevard)	Santa Teresa, New Mexico

This would apply a deduction to intrastate transportation for relatively few carriers.

PERFORMANCE IMPLICATIONS

The LFC tax policy of accountability is nominally met with the bill's requirement that TRD report annually to an interim legislative committee regarding the data compiled from the reports from taxpayers taking the deduction and other information to determine whether the deduction is meeting its purpose. However, the bill does not indicate the purpose of the deduction, does not establish goals, targets or milestones. To date, the requirement for separate reporting of GRT deductions has not been effective because there is no penalty for failure to identify the specific provision of law creating a deduction.

TECHNICAL ISSUES

TRD points out a potentially major technical problem with the geo-specific provisions of this bill:

> This bill would appear to violate the dormant commerce clause of the federal constitution, which prohibits states from discriminating against interstate commerce by treating businesses located outside of the state less favorably than businesses located inside the state. The bill provides a tax deduction only for taxpayers performing transportation in the state if the taxpayer's principal place of business is located in New Mexico. This would clearly disfavor businesses that may perform the same transportation service but are located outside New Mexico. Nor does the requirement that the business be located within a certain distance of a port of entry change the fact that the principal place of business requirement is likely to be held to discriminate against out-of-state businesses.

However, LFC staff does not believe this objection is credible. Transportation in interstate commerce is already deductible from gross receipts pursuant to the provisions of 7-9-56 NMSA 1978

> A. Receipts from transporting persons or property from one point to another in this state may be deducted from gross receipts when such persons or property, including any special or extra service reasonably necessary in connection therewith, is being transported in interstate or foreign commerce under a single contract.
> B. Receipts from handling, storage, drayage or packing of property or any other accessorial services on property, which property has moved or will move in interstate or foreign commerce, when such services are performed by a local agent for a carrier or by a carrier and when such services are performed under a single contract in relation to transportation services, may be deducted from gross receipts.

Thus, the discrimination is not against interstate commerce, but against other intrastate carriers not located within the 35 mile zone. The bill does not provide a reason for this discrimination. It may be based on an economic development argument, but, if so, then that reason should be stated in the provisions of the bill.

In the 1990's, New Mexico established a differential rate for ethanol enhanced gasoline that required the ethanol to be produced in New Mexico from grain grown on New Mexico farms. After a few years of effect, the state was sued by an out-of-state manufacturer of ethanol. The case went to the state supreme court and the state lost on interstate commerce grounds. The remedy was to repeal the differential rate, rather than allow the differential rate to the out-of-state manufacturer.[1]

This bill does not contain a delayed repeal date. LFC recommends adding a delayed repeal date.

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

The provisions of this bill violate equity principles.

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

1. **Vetted**: The proposed new or expanded tax expenditure was vetted through interim legislative committees, such as LFC and the Revenue Stabilization and Tax Policy Committee, to review fiscal, legal, and general policy parameters.
2. **Targeted**: The tax expenditure has a clearly stated purpose, long-term goals, and measurable annual targets designed to mark progress toward the goals.
3. **Transparent**: The tax expenditure requires at least annual reporting by the recipients, the Taxation and Revenue Department, and other relevant agencies.
4. **Accountable**: The required reporting allows for analysis by members of the public to determine progress toward annual targets and determination of effectiveness and efficiency. The tax expenditure is set to expire unless legislative action is taken to review the tax expenditure and extend the expiration date.
5. **Effective**: The tax expenditure fulfills the stated purpose. If the tax expenditure is designed to alter behavior – for example, economic development incentives intended to increase economic growth – there are indicators the recipients would not have performed the desired actions "but for" the existence of the tax expenditure.
6. **Efficient:** The tax expenditure is the most cost-effective way to achieve the desired results.

The provisions of this bill do not conform with the LFC tax expenditure policy principles.

LG/gb/sb

[1] 7-13-4.2. Deduction; ethanol blended fuel produced using New Mexico agricultural products.
A. In computing the gasoline tax due, ethanol blended fuel manufactured exclusively in New Mexico shall be deducted from the total amount of gasoline received in New Mexico in the following amounts and during the specified periods, provided that at least fifty percent of the agricultural feedstocks by volume used in fermentation are produced in New Mexico and provided further that satisfactory proof is furnished to the department:
(1) from July 1, 1987 through June 30, 1988, eight cents ($.08) per gallon;
(2) from July 1, 1988 through June 30, 1989, eight cents ($.08) per gallon;
(3) from July 1, 1989 through June 30, 1990, three cents ($.03) per gallon; and
(4) from July 1, 1990 through June 30, 1991, two cents ($.02) per gallon.
History: 1978 Comp., § 7-13-4.2, enacted by Laws 1983, ch. 225, § 3; repealed by Laws 1988, ch. 165, § 1