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FISCAL IMPACT REPORT

SPONSOR <u>Shendo/Harper</u>	LAST UPDATED <u>3/18/23</u>
SHORT TITLE <u>Tax Administration Changes</u>	ORIGINAL DATE <u>2/14/23</u>
	BILL NUMBER <u>Senate Bill 146/aSTBTC/aSFC</u>
	ANALYST <u>Torres</u>

REVENUE* (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY23	FY24	FY25	FY26	FY27		
		Indeterminate but unsubstantial			Recurring	General Fund
		Indeterminate but unsubstantial			Recurring	Local Governments

Parenthesis () indicate revenue decreases

*Amounts reflect most recent version of this legislation.

Sources of Information

LFC Files

Responses Received From

Taxation and Revenue Department (TRD)
 Administrative Hearings Office (AHO)
 New Mexico Attorney General (NMAG)

SUMMARY

Synopsis of SFC Amendment to Senate Bill 146

The Senate Finance Committee amendment to Senate Bill 146 strikes Sections 1 and 2, eliminating the two sections in the original bill that increased the minimum amount of delinquent tax that TRD may assess from \$25 to \$50 and the provision that limited taxpayers from protesting amounts under \$50.

Synopsis of STBTC Amendment to Senate Bill 146

The Senate Tax, Business and Transportation Committee (STBTC) amendment adds language to Section 7-38-22 NMSA 1978 allowing the parties to agree to an alternative service method for the notice of hearing other than certified mail. The amendment also clarifies Section 9 of the bill specifying that this section is in regard to the Administrative Hearings Office.

Synopsis of Senate Bill 146

Senate Bill 146 (SB146) proposes changes to the tax code as recommended by the Taxation and

Revenue Department (TRD). The bill contains the following provisions:

Section 1 increases the minimum amount of delinquent tax that TRD may assess from \$25 to \$50. In turn, Section 2 provides that taxpayers may only protest disputed amounts over \$50.

Section 3 provides a taxpayer's tax credit application must be complete before the TRD timeline to review and approve or deny the credit begins. Because TRD will have a complete application for its entire review period, the bill also reduces TRD's review time from 180 to 120 days.

Section 4 incorporates newer fraud technologies into New Mexico's criminal tax fraud statute. Electronic sales suppression devices called "zappers" and software called "phantomware" can be used to falsify records of a cash register or point-of-sale device to artificially lower a business' sales to evade taxation, and this bill provides that tax fraud includes the intent to evade or defeat tax by knowingly selling, licensing, purchasing, installing, transferring, manufacturing, developing or possessing these devices and software.

Section 5 clarifies protests of property valued by county assessors are heard before the county protest board.

Section 6 adds new material to specify protests of property valued by TRD's Property Tax Division go to the Administrative Hearing Office (AHO) or to a district court if a refund is sought. This sets out the procedure if TRD and the property owner cannot resolve the classification or valuation of the property informally.

Section 7 allows for property owners who did not report their properties to TRD, but who were subsequently valued by TRD's Property Tax Division (omitted property) to have the same protest rights as taxpayers who reported their property. These same rights apply whether the protest is before the AHO or in district court.

Sections 8 and 9 amend Section 7-38-28 NMSA 1978 and create new material to clarify appeals of county-assessed property go to the district court. Appeals of state-assessed property by either the property owner or TRD to go to the Court of Appeals. This will make the appeal process for TRD uniform with the appeal process under the Tax Administration Act for all other taxes administered by TRD.

The effective date of this bill is July 1, 2023.

FISCAL IMPLICATIONS

The Administrative Hearing Office cautions:

In a previous version of the bill in 2021, the TRD indicated to AHO that the addition of the omitted property to the list of potential protests might increase the hearing case load by approximately six-cases a year. With the information in 2021, AHO did not anticipate this would add much additional cost, and thus listed no fiscal impact at that time. However, subsequent experience in property tax valuation protests has caused AHO to reconsider the potential fiscal impact of the addition of omitted property tax valuation protests under this proposed legislation. These hearings have proven to be lengthy, involve competing expert witnesses, and litigious (*see performance implications section for more details*). Even a small increase in these cases will lead to an increased strain on the timeline of the tax docket. The minor change to the assessment threshold in the bill is

unlikely to have any significant impact on the hearing docket at AHO. However, AHO anticipates that the increased property tax protests under this bill could result in an 1/3 increase to a hearing officer docket timeframe (time for deciding prehearing motions, hearing preparation, conducting merits hearing, writing decision, and preparing record proper for appeal). *Such increase in the tax hearing docket might be absorbable with current staffing resources, but if the hearing load under this bill is larger than TRD projects or if AHO is also given additional hearing duties through other bills this session, the cumulative effect could lead to the need for an additional hearing officer reoccurring costs and one-time costs.*

Section 4: The potential loss of government revenue from “zappers” and “phantomware” is unknown. Incorporating those technologies in New Mexico’s tax fraud statute may potentially increase GRT received by the state and local governments. The IRS and other financial investigative entities have identified use of such software throughout the state.

Provisions of the bill amending the credit application process will reduce confusion on the part of taxpayers and greatly enhance TRD’s ability to administer credit applications in a fair and timely manner. This is expected to decrease the volume of protests of tax credit denials that were never fully supported by the taxpayer, which will decrease TRD staff time responding to protests. The Information Technology Division (ITD) of TRD will implement changes into GenTax, the tax system of record, for the change in credit review time from 350 hours or about two months. This will require approximately \$19,439 of staff workloads cost.

SIGNIFICANT ISSUES

The Taxation and Revenue Department explains:

Section 3: Regarding amendments to the tax credit application process in Section 7-1-29.2 NMSA 1978, current law provides that if a taxpayer applies for a tax credit, the credit is deemed approved if the taxpayer does not receive an approval or denial within 180 days from applying for the credit with TRD. Because current law provides no requirements that ensure a taxpayer’s credit application is complete, TRD may spend some or all of its 180-day review period attempting to obtain a complete credit application that provides all the information needed to approve or deny the credit. This bill will ensure TRD has its entire statutory window to consider a complete application, and as a result, the statutory review time can be reduced from 180 to 120 days. This bill provides details on what must be submitted to start the timeline so that the clock only begins to run when TRD has a complete application.

Section 4: Sales suppression devices such as “zappers” and “phantomware” allow fraudulently recorded sales transactions to appear as perfectly normal sales transactions. Customers receive accurate receipts of goods or services during the normal day of business; however, at the end of the day, a portable USB device is plugged into the electronic Point-Of-Sale (POS) system to remove given dollar amounts in sales from the day’s receipts. The zapper re-totals and recalculates the receipts to reduce tax liabilities that the business owner is obligated to pay. The business keeps two sets of books: one set prepared for the tax authorities, the other set to show the real earnings of the business. The bill clarifies the implications of a person knowingly purchasing, possessing, installing, using, selling, licensing, transferring, manufacturing or developing sales suppression devices, software, zappers or phantomware to strengthen New Mexico’s

ability to prosecute such crimes. Other states have enacted similar legislation. TRD believes this software is likely currently being utilized in New Mexico. By expanding the statute to unambiguously disallow the use of sales suppression devices, TRD's Tax Fraud Investigations Division (TFID) can criminally charge taxpayers found using these devices to alter taxable income and receipts.

Sections 5 and 6: Section 5 clarifies that protest of property valued by the county assessor shall be brought before the county protest board. Conversely, Section 6 provides that when property is classified and valued by TRD's Property Tax Division (PTD), if the property owner and PTD cannot resolve the protest informally, the property owner may protest by filing a petition of protest with the AHO or paying the property tax due and filing a claim for refund in a district court.

Section 7: Provides clarification around how to protest PTD's valuation of omitted assets (assets that were not reported by the owner). Current statute is silent on protests of state-assessed omitted property. This proposal would set out the avenues a property owner has available to protest valuation and classification of omitted state-assessed property. This change ensures that valuation protests of state-assessed property — whether reported or omitted— are treated consistently.

Under Section 7-38-76 NMSA 1978, county assessors, treasurers and TRD have the authority and the duty to bill for and collect the property taxes for property that was subject to property taxation but were omitted (i.e. not reported by the property owner) from property tax schedules. Properties omitted from property tax schedules are referred to as omitted property.

In classifying and valuing property, TRD has exclusive jurisdiction over state-assessed property, as defined under Section 7-36-2(B) and (C) NMSA 1978. This jurisdiction includes the authority to issue notices of valuation for omitted assets.

Sections 8 and 9: This change will allow for clarification and guarantee TRD the ability to appeal an adverse decision from the AHO on property tax matters. These changes allow the owners of residential and commercial property assessed by county assessors the statutory right to appeal a decision to the county protest boards and appeal any adverse decision to a district court under Section 7-38-28 NMSA 1978. The change allows for either the property owner or TRD to appeal the classification or valuation of property determined by either the AHO or a district court to the court of appeals. Currently, in the event of an adverse AHO decision and order, TRD has no statutory right of appeal but must seek a writ of certiorari in district court.

The New Mexico Attorney General notes:

Section 9 of SB146 does not specify any further avenue for appeal on a writ of certiorari after a direct appeal of a hearing officer's order to the court of appeals. This is different from the ordinary procedure for administrative appeals, which proceed through the district court on direct appeal, and to the court of appeals on a writ of certiorari. If any further appellate review is intended beyond a direct appeal of the hearing officer's order to the court of appeals, that may need to be clarified in the statute.

If the intent of the bill is to allow writ of certiorari review of an appeals decision of the

court of appeals regarding an order of a hearing officer, Section 9 of the bill might have the a new Subsection D added between current Subsections C and D of Section 9. The proposed language for that subsection below mirrors the procedural language of Section 39-3-1.1 regarding ordinary administrative appeals:

[D. A party to the appeal to the court of appeals may seek review of the court of appeals decision by filing a petition for writ of certiorari with the supreme court, which may exercise its discretion whether to grant review.]

Again, it is unclear whether the intent of the bill is to divest the supreme court of certiorari review of appeals of hearing officer orders. If that is the intent of the bill, no amendments are necessary.

PERFORMANCE IMPLICATIONS

Although six additional property tax protest cases annually is a low volume of total new cases, recent experience has shown AHO that when property tax valuation protests occur, they tend to be lengthy hearings lasting approximately a week with competing expert witness testimony. Moreover, recent experience has also shown to AHO that the litigants in this property tax and tax arena have demonstrated a reluctance to accept the legal analysis of both AHO and the Court of Appeals on questions of law, preferring to relitigate every issue. That reluctance leads to repetitive, inefficient, and contentious litigation, frequent prehearing motions, a lengthy hearing process, and an extensive record with many factual and legal issues that must be resolved either in complex prehearing orders or in the final decision. Additionally, the frequency of appeals of tax protests in general, including in the property tax context, leads to extensive extra hearing officer and staff work in compiling, maintaining, and submitting the record proper to the appellate court. Such extensive and complex work could make it difficult for AHO to meet existing tax hearing performance measures and statutory deadlines with existing staffing.

TECHNICAL ISSUES

The Administrative Hearings Office suggests:

- 1) In both the title and text of Section 9, the bill uses the generic term “hearing officer,” presumably referring a hearing officer of the administrative hearings office given the apparent purpose of that new section. However, the use of this generic term could still be confusing, because a County Valuation Board may also use a hearing officer as part of their valuation protest hearings. If the purpose of Section 9 is to establish that appeals of the decisions of Administrative Hearings Office go the Court of Appeals, then Section 9 should clarify that it is referring to decisions of the administrative hearings office rather than reference a generic hearing officer.

This section was written before TRD indicated that an amendment addressing this concern was drafted. It is still being included as an explanation related to that pending amendment.

- 2) In Section 7 (C) of the bill, p. 15, lines 11-16, the mailing provision of notice of hearing is being updated to reflect current practice. Similarly, a provision should be added to that section permitting the parties to agree with some form of notice other than certified mail, which would permit with the parties’ consent electronic forms of notice. This recognizes that parties often communicate electronically on these matters and often

the parties prefer videoconference or hybrid hearings. Videoconference and hybrid hearings lend themselves particularly well to electronic notice of hearing in addition to traditional mailing methods.

This section was written before TRD indicated that an amendment addressing this concern was drafted. It is still being included as an explanation related to that pending amendment.

3) In Section 7 (D) of the bill, p. 15, lines 17-18, the bill updates the statute to replace director with secretary for the purposes of indicating who may provide for an informal conference. This entire section was written before AHO was even an agency, and thus there was never a reason to include AHO in this language. However, since subsequent statutory changes have made AHO the independent agency responsible for adjudicating these disputes, AHO's hearing officer should also be included in this section as a person in addition to the secretary with authority to permit an informal conference before the hearing. It is well understood in any legal hearing process that that the adjudicator (whether that be a judge, arbitrator, or hearing officer) has authority as part of docket and case management to direct (with appropriate respect for its role as the neutral decisionmaker) the parties to engage in informal conferences, prehearing conferences, discovery meetings, scheduling hearings, and similar preliminary steps in order to facilitate a fair and efficient hearing process.

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