ISSUES FOR HEARING
Economic and Rural Development Committee
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NEW MEXICO TAX EXPENDITURES

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SUMMARY:

- Tax expenditures are government spending programs authorized through the tax code. Although tax expenditures are an important component of the state's annual budget, the state does not have a systematic means of reporting and analyzing their effects.

- Per Executive Order 2011-071 the Taxation and Revenue Department will be the lead agency in preparing an annual tax expenditure budget.

- Tax expenditures can be an efficient means of targeting selected populations for benefits, and also of influencing the decisions of private individuals to further the goals of public policy. New Mexico's tax code has hundreds of tax expenditures. Each of New Mexico's major tax programs contains numerous tax expenditures that affect virtually all NM taxpayers.

- These programs give people, groups and businesses special tax credits, deductions, exclusions, exemptions, deferrals, and preferential rates in support of various government policies. Tax expenditures are not limited to economic development incentives. Some of these programs help people save for retirement, buy a home, or pay for college; others encourage companies to invest in green energy technologies; they even subsidize corporations that drill for oil or purchase real estate; and much more.

- Tax expenditures can be difficult to define and identify. In preparing the tax expenditure budget the key is to properly define a "Tax Expenditure." Tax expenditures do not include provisions that define the proper scope of the tax base, prevent double taxation or avoid interference in interstate commerce.

- A good tax expenditure report is easily accessible by being published annually and on the Web, broad in scope and has all tax expenditures listed, detailed in that it includes current and future cost, description of, and who benefits from each tax expenditure and includes analysis of intended purpose and success in accomplishing that purpose.

- Consideration should be given to a comprehensive bill that sunsets all existing tax incentives.

HEARING BRIEF

DATE: November 4, 2011

LFC TAX POLICY PRINCIPLES:

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

To calculate the exact cost of GRT deductions and exemptions requires them to be listed on tax returns. This is burdensome for taxpayers and TRD.

LFC has included a list of tax expenditures in volume 1 of the annual budget recommendation and plans to continue this practice until a formal tax expenditure budget is prepared by TRD.

The process of appropriating should include a side by side analysis of line item expenditures and a comparison of foregone revenue.

<u>Elements of a Good Tax Expenditure Report.</u> Although the best practice would be to incorporate tax expenditures into the annual budgetary process, or appropriation bill; most states publish a separate tax expenditure budget report. A good tax expenditure report is a difficult undertaking. Calculating foregone revenue is only the first step. To answer questions like whether the expenditure is achieving its goals requires detailed analysis. Objectivity is required. Agencies or individuals with a vested interest in promoting a program may not provide a reliable assessment of program effectiveness.

To achieve its goals of improving transparency, encouraging accountability, and saving money, a tax expenditure report should have the features listed below:

1. Accessibility. The report should be:
   a. Published regularly.
   b. Incorporated into the budget process.
   c. Available on the Web.
2. Scope. The report should include:
   a. Tax expenditures related to all taxes.
   b. Explicit and implicit tax expenditures.
   c. Tax expenditures enacted by the state that affect local government.
3. Detail. The report should include:
   a. The cost of the tax expenditure, using current data.
   b. The cost in future years, to allow comparison with other proposed expenditures.
   c. A description of the tax expenditure.
   d. The relevant legal citation and year of enactment.
   e. Detail on the taxpayers who benefit from the tax expenditure.
   f. Separate reporting for the state and local revenue losses, where applicable.
4. Analysis. The report should:
   a. Classify tax expenditures using the same categories as direct spending.
   b. State the intended purpose of the tax expenditure.
   c. Evaluate the extent to which that intended purpose has been accomplished.
   d. Analyze the distribution of benefits by income level and size of business.

Developing such a report will require that taxpayer beneficiaries provide more information than they do now, and the TRD be authorized to release the information. A balance will have to be struck between the need for public information and the taxpayer's need for confidentiality.