



Interim Revenue Stabilization and Tax Policy Committee

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2013 Interim Legislative Agenda Items

Income Tax

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- **Statewide chamber of commerce**
- **Mission:**

To enrich the lives and prosperity of New Mexicans through a vibrant business climate by effective advocacy and education
- **Broad cross section of business community**
 - **Large and small**
 - **Diverse businesses**
- **Member driven, bottom-up semi-annual policy development process**

2013 INTERIM LEGISLATIVE AGENDA

ACI SUPPORTS

- Single weighted sales factor apportionment for corporate income tax
- Elimination of the "throwback rule" for the New Mexico corporate income tax apportionment sales factor
- Reducing the highest corporate income tax rate from 7.6% to 4.9% to mirror the highest personal income tax bracket
- Clarification that New Mexico's treatment of corporate income tax net operating losses is governed by provisions of the Internal Revenue Code and associated regulations
- Stable and predictable tax system
- Fair tax administration

2013 INTERIM LEGISLATIVE AGENDA

ACI SUPPORTS

- Replacing Taxation and Revenue Department internal hearing officers with independent, external hearing officers
- A comprehensive state economic development plan
- Transparency and accountability for New Mexico tax incentives in a manner that protects taxpayer confidentiality and proprietary information

ACI OPPOSES

- Elimination of alternative corporate income tax filing methods for corporate groups and requiring unitary combined group reporting

Single Weighted Sales Factor Apportionment

- Apportionment determines portion of business operations income taxable by New Mexico
- Current “three factor” method looks to states in which taxpayer has:
 - Employees
 - Personal and real property
 - Customers (tangible personal property) or cost of performance (services and intangible personal property)
- Single sales factor apportionment looks only to state of customer

Single Weighted Sales Factor Apportionment

- Single sales factor favorable for businesses that sell to out of state customers
- Brings “new” money into the New Mexico economy
- Broad-based and does not pick winners and losers
- Attracts business investment and job creation

Single Weighted Sales Factor Apportionment

NATIONAL BUSINESS

Base Case	<u>Prop.</u>	<u>Payroll</u>	<u>Sales</u>	<u>NM %</u>
Three Factor	5%	5%	1%	4%
Single Factor			1%	1%
Double NM Investment				
Three Factor	10%	5%	1%	5%
Single Factor			1%	1%
Double NM Payroll				
Three Factor	5%	10%	1%	5%
Single Factor			1%	1%
Double NM Payroll & Investment				
Three Factor	10%	10%	1%	7%
Single Factor			1%	1%

Single Weighted Sales Factor Apportionment

REGIONAL BUSINESS

Base Case	<u>Prop.</u>	<u>Payroll</u>	<u>Sales</u>	<u>NM %</u>
Three Factor	25%	25%	25%	25%
Single Factor			25%	25%
Double NM Investment				
Three Factor	50%	25%	25%	33%
Single Factor			25%	25%
Double NM Payroll				
Three Factor	25%	50%	25%	33%
Single Factor			25%	25%
Double NM Payroll & Investment				
Three Factor	50%	50%	25%	42%
Single Factor			25%	25%

Single Weighted Sales Factor Apportionment

LOCAL BUSINESS

All Cases	<u>Prop.</u>	<u>Payroll</u>	<u>Sales</u>	<u>NM %</u>
Three Factor	100%	100%	50%	83%
Single Factor			50%	50%

All Cases	<u>Prop.</u>	<u>Payroll</u>	<u>Sales</u>	<u>NM %</u>
Three Factor	100%	100%	15%	72%
Single Factor			15%	15%

Sales Factor “Throwback Rule”

- Increases New Mexico sales factor
- Artificially attributes sales to New Mexico when state of customer has no jurisdiction to tax customer
 - No seller physical presence in customer state
 - Seller has only sales force in customer state
- Increases New Mexico corporate income tax liability for those who sell to customers in other states
- Would thwart goal of adoption of single sales factor apportionment

Reduce Top Corporate Income Tax Rate

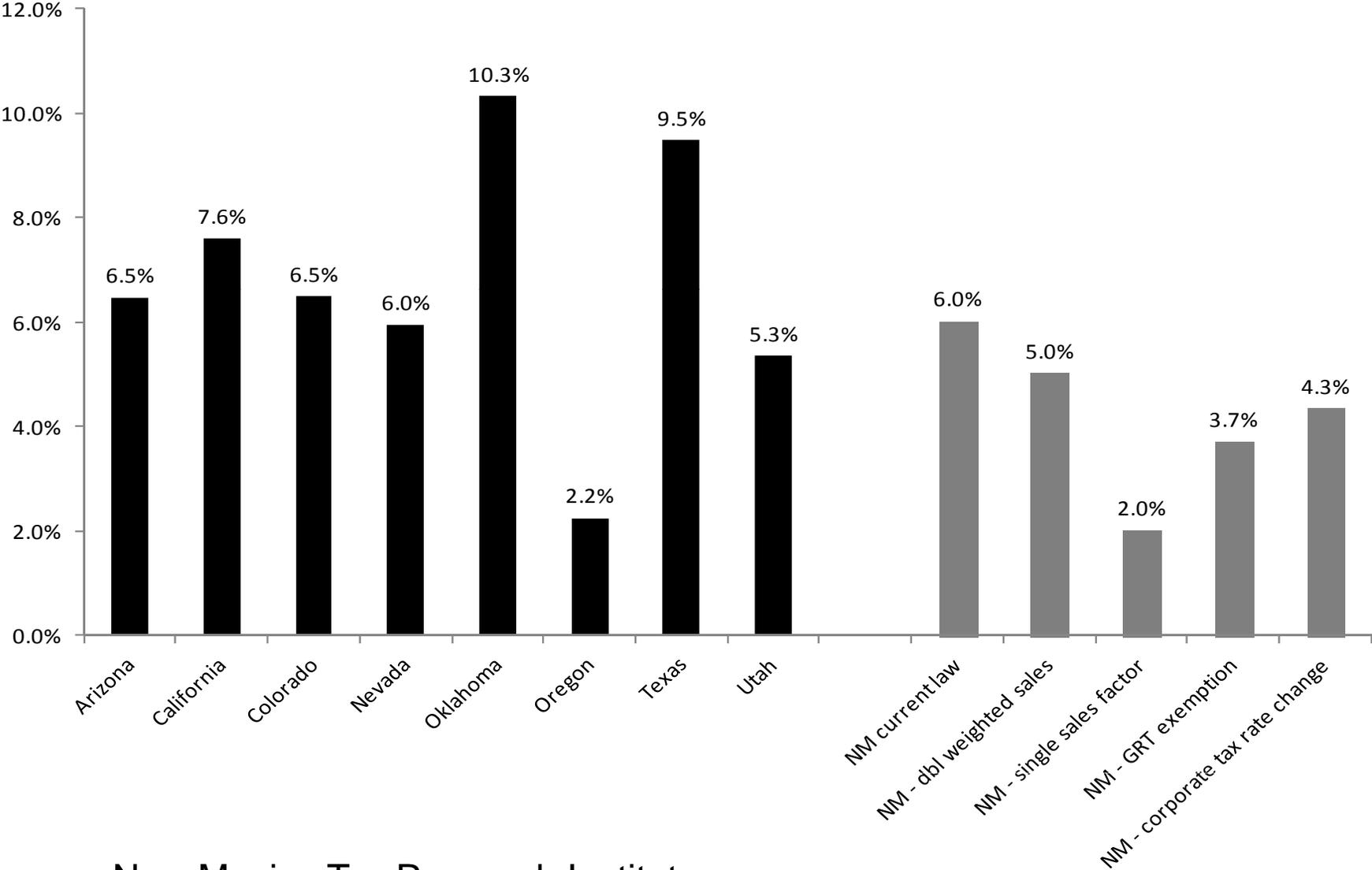
From 7.6% to 4.9%

- Most small businesses pay personal income tax at 4.9%
 - LLC, Partnership owners
 - Sole Proprietorship
- New Mexico not rate competitive with neighbors for corporate income tax

Reduce Top Corporate Income Tax Rate From 7.6% to 4.9%

Texas	1% (of gross receipts)
Nevada	0%
Colorado	4.63%
Utah	5.00%
Oklahoma	6.0%
Arizona	6.97% (4.9% by 2016)
New Mexico	7.60%
California	8.84%

Comparison of After-Tax Effective Tax Rate for Comparison States and New Mexico under Selected Policy Options



Source: New Mexico Tax Research Institute

Clarify New Mexico Treatment of Corporate Income Tax Net Operating Loss Deduction

- Net operating losses, by statute, are defined as they are for federal income tax purposes
- New Mexico statutes do not expressly address whether New Mexico follows federal rules for use of net operating loss deduction
- Taxation and Revenue Department policy on audit tends to not follow federal rules regarding use of net operating loss deduction after a merger or acquisition
- Uncertainty and confusion
- New Mexico statute allows 5 year carryforward
- Federal law allows 20 year carryforward
 - Arizona just went to 20 year carryforward

Stable and Predictable Tax System

- Businesses prefer to operate in a stable and predictable tax system
- Uncertainty deters investment that can create jobs in favor of investment in states with a more predictable tax environment
- New Mexico suffers from a perception that relative to other states it has an unstable and unpredictable tax system
 - Legislation
 - Incentive Tinkering
 - Corporate income tax reporting methods
 - Administration

Fair, Predictable, Transparent and Efficient Tax Administration

- Taxation and Revenue Department establishment of tax policies and practices that are not retroactive to periods before adoption
- Effective advance notice to taxpayers of Taxation and Revenue Department tax policies and administration
- Establishing tax policies and practices in a transparent public process rather than through assertion of positions during an audit and/or litigation
- Effective opportunities to address auditor findings with the Taxation and Revenue Department without the need for taxpayers and the Department to engage in time consuming and costly litigation

Independent Hearing Officers for Challenges to Taxation and Revenue Department Actions

- Currently, hearing officers assigned to hear tax protests are employees of the Taxation and Revenue Department
- New Mexico one of the few states that do not have external independent hearing officers
- Leads to perception of bias and lack of impartiality
- Reduces confidence in stability of New Mexico tax administration and policy

New Mexico Economic Development Plan

- **New Mexico has no comprehensive strategic plan for economic development**
 - Haphazard, piecemeal legislation
 - Too often parochial, political, vested and special interests control rather than what is best for New Mexico
 - Tax legislation often inequitably and narrowly picks winners and losers for fear of an adverse FIR
 - Tax legislation that is not necessarily effective
 - Over-reliance on unduly complex and difficult to administer incentives
 - Little or no effort to establish statewide priorities

New Mexico Economic Development Plan

- **New Mexico needs to evaluate what types of businesses that it can and should *realistically* nurture or attract and retain that are well matched to, among other things:**
 - Work force
 - Education
 - Infrastructure
 - State and local financial resources
 - Natural resources
 - Urban and rural needs and economies
 - Regional, national and international competition
- **Establish priorities for doing so**
- **Establish an accountable action plan**
- **Particularly important as New Mexico faces reduction in federal funds**

Tax Incentive Transparency and Accountability

- ACI supports meaningful tax incentives
- ACI generally supports efforts to evaluate the effectiveness of tax incentives
- ACI has concerns about prior and proposed legislation that would make confidential and proprietary information of incentive recipients public
 - New Mexico less likely to attract business if taxpayer information becomes public
 - New Mexico's tax system depends on voluntary compliance
 - Risk of erosion with loss of confidentiality

Tax Incentive Transparency and Accountability

- The difference between good tax policy and a tax incentive/expenditure can be in the eye of the beholder
- Be cautious about so-called “tax expenditure” budgets
 - Often misunderstood
 - Sometimes framed to advance narrow special interest agendas rather than good tax policy
- Not all exemptions and deductions true tax expenditures
 - Broad gross receipts tax pyramiding deductions (e.g. resale) make for a sound tax system
 - Gross receipts tax exemption for wages necessary (otherwise every citizen would have to file return and pay gross receipts tax)

Tax Incentive Transparency and Accountability

- Other exemptions, deductions and credits reflect social, economic development/job creation policy choices that deserve a cost/benefit analysis:
 - Food
 - Medical
 - Renewables
 - Film
 - R&D
 - Rural
 - Manufacturing
 - Ect.

Mandatory Unitary Combined Corporate Income Tax Reporting

- Three methods of corporate income tax filing intentional since the 1960's to attract investment to New Mexico
 - Initially administratively
 - Later, by statute
- Elimination of filing options would make New Mexico less competitive with other states for new investment
- Changing filing methods for businesses already investing in New Mexico is fundamentally unfair

Mandatory Unitary Combined Corporate Income Tax Reporting

- Corporate income tax generates roughly 4-5 % of New Mexico tax revenue
- Unitary combined filing is very complex and generates constant disputes and litigation
- Significant misunderstanding as to operation of mandatory unitary combined reporting and impact on corporate income tax liability
- Studies and experiences in other states indicate likely no significant revenue increase and potential for decrease
- Mandatory unitary combined filing could, depending on facts, have adverse impact on New Mexico based business, just as much as out of state based business



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