

Final Report
of the
Blue Ribbon Tax Reform Commission
October 2003

BLUE RIBBON TAX REFORM COMMISSION

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BLUE RIBBON TAX REFORM COMMISSION

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Executive Summary

The Blue Ribbon Tax Reform Commission was created to deal with a widespread feeling that New Mexico's tax system no longer fully meets the state's diverse needs. The commission was created by Laws 2003, Chapter 77 (HB 168). The commission's general charge was to:

develop recommendations for reform of New Mexico's tax laws to establish a balanced tax system that provides maximum economic development benefits and maintains necessary government services at an appropriate level.

The 23 members of the commission (10 members of the legislature and 13 public members) organized themselves into five committees to better deal with the vast territory to be covered in the short time available.

The commission's general goal was to align New Mexico's taxes more closely with its economy and its future. Members also hoped to achieve progress with several specific problems.

Many of the specific concerns centered on the single largest source of revenue for the state and its municipalities, the gross receipts tax. Chief among the concerns was the extent of pyramiding in this tax, particularly on the services side. Issues arose in other revenue programs as well, for example:

- The wide menu of choices built into the corporate income tax, which could be taken as an economic development incentive or as an unnecessary leakage of revenue.
- The commission's specific charge to re-examine the cuts in the personal income tax made earlier in the year.
- Burdensome administration of the tax law.

The commission resolved to tackle these problems through analysis based on tax principles.

Adequacy is a cardinal principle of taxation; taxes that do not raise the required revenues are failures no matter how fair or easy to administer they may be. Determining what revenue is required is the quintessential question of government. The commission recognized that even attempting to frame a general answer lay well beyond its mandate unless a solid case could be laid before it on specific programs. The commission took its mission as reform rather than

adjusting the total tax burden substantially. Reform of a tax system does not imply that the end result will either raise or reduce revenues in the short run.

The commission formally developed 196 separate proposals to alter the tax system. (See Appendix B-1 for a complete listing.) Of these, the commission adopted 71.

Highlights of the adopted recommendations:

- Expansion and enrichment of the low-income comprehensive tax rebate table and an added income tax personal exemption of up to \$3,000 for families below the median income level for their filing status.
- New gross receipts tax deduction for health practitioners for receipts from managed health care contracts and Part C Medicare payments.
- Gross receipts deduction for for-profit hospitals expanded from 50 percent to 100 percent to treat virtually all hospitals similarly.
- Restoration of some progressivity in the income tax, capping of the state capital gains deduction.
- Dropping the highest corporate income tax rate from 7.6 percent to 6.4 percent, then compressing the three-step tax table to two steps. Corporations would be required to file on a combined unitary basis.
- Increasing the gasoline and special fuel (diesel) tax rates, vehicle registration fees and other fees to increase funding for state and local road funds.

The commission made no recommendations in these areas:

- Gross receipts tax on food. For a variety of reasons, the commission believed that expanding the low-income comprehensive tax rebate table and establishing a new personal exemption was preferable to reducing or eliminating the gross receipts tax on receipts from selling groceries.
- Personal income tax rates. Although the commission studied delaying or eliminating the later phases of the income tax rate cut enacted earlier in 2003 and whether to restructure those phased-in cuts, it decided not to make a recommendation on this issue.
- Gross receipts tax exemption for nonprofit organizations. Other than recommending a change in reporting for the larger organizations, the commission decided it did not have the information to separate nonprofits thought to be competing with for-profit businesses from those engaging in strictly eleemosynary activities.
- Liquor excise tax. This tax is but a small part of a much larger issue of alcohol abuse in this state. The commission agreed that this is a critical issue for the people of New Mexico but did not deem it appropriate for this commission, but rather felt the full legislature and the governor needed to address it.

Introduction

The Blue Ribbon Tax Reform Commission was created to deal with a widespread feeling that New Mexico's tax system no longer fully meets the state's diverse needs. A legacy mainly of the reform efforts of the late 1960s and 1970s, the tax system may have slowly gotten out of step with the state and national economies. Piecemeal updates aimed at particular problems were no longer enough; a deep look at the fundamental relationships in the system was necessary to re-align the tax system with the state's evolving goals.

Nationally, two significant trends added pressure to tackling the issues now, rather than later. First, the federal government launched major structural changes in the personal income tax upon which the state's tax is based and completely phased out the estate tax. Second, the states themselves have created an apparently viable reformulation and standardization of the sales tax that is intended to resolve a decades-long struggle with sales by remote sellers. The ability of vendors virtually anywhere in the world to do business in New Mexico is the most obvious symptom of the changes being wrought by the rapid penetration of telecommunications and technology products into both businesses and households.

Newly elected Governor Bill Richardson's drive to bring New Mexico fully to the attention of the business world and to bring high-paying jobs to the state also provided needed impetus.

a. Mission and Authority

The Blue Ribbon Tax Reform Commission was created by Laws 2003, Chapter 77 (House Bill 168). The commission's general charge was to:

develop recommendations for reform of New Mexico's tax laws to establish a balanced tax system that provides maximum economic development benefits and maintains necessary government services at an appropriate level.

More specifically, the act instructed the commission to:

- (1) examine the tax system, identify its strengths and weaknesses and consider a broad range of improvements that could be made to modernize it and make it more conducive to economic growth;
- (2) examine the personal income tax reductions approved during the first session of the forty-sixth legislature and determine if any changes are necessary and what those changes should be; and
- (3) report its findings and recommendations to the governor and the New Mexico Legislative Council by September 1, 2003. (This deadline was twice extended, first to September 30, 2003 and, then, to October 2003.)

b. Members

By the middle of April, Governor Bill Richardson, Senate President Pro Tempore Richard M. Romero and Speaker Ben Lujan had appointed the 23 members of the commission.

Members of the House of Representatives appointed by Speaker of the House Ben Lujan:

Representative Janice Arnold-Jones
Representative Irvin Harrison
Speaker Ben Lujan
Representative Thomas C. Taylor
Representative Donald L. Whitaker

Members of the Senate appointed by President Pro Tempore Richard M. Romero:

Senator Manny M. Aragon
Senator Carroll H. Leavell
Senator Cisco McSorley
Senator Leonard Lee Rawson
Senator John Arthur Smith

Public members appointed by the speaker of the house and the president pro tempore:

Mr. Ron Morgan, attorney
Mr. Murray Ryan, former legislator, retired

Public members appointed by Governor Bill Richardson:

Mr. Jerry Sandel, chairman, former legislator, oil and gas industry
Mr. Norman P. Becker, CEO, Lovelace Sandia Health System
Governor Garrey Carruthers, dean, College of Business Administration
and Economics, NMSU
Mr. William F. Fulginiti, New Mexico Municipal League
Ms. Gail Haynie, Public Service Company of New Mexico
Ms. Debbie Hays, county manager, Sandoval County
Mr. Bill King, rancher
Mr. Matt C. Martinez, general manager, KNMW-KMDZ Radio
Dr. Brian McDonald, retired, executive director, UNM Bureau of Business
Research
Mr. Fred Nathan, executive director, Think New Mexico
Governor Bruce Sanchez, former governor, Santa Ana Pueblo;
executive director, Santa Ana Gaming Regulatory Commission

c. Organization of the Commission

The extent of topics to be covered and the relatively short time available to the commission lead to the creation of five committees to pursue the commission's business.

Steering Committee. The charge of this committee was to ensure the business of the commission was conducted in an orderly manner and that the commission discharged all of the duties mandated by law.

Jerry Sandel, chairman
Senator Aragon
Speaker Lujan
Chairs of the four other committees
Mr. Becker
Governor Carruthers
Senator Leavell
Dr. McDonald

Economic Development Committee. This committee reviewed taxation of business-to-business transactions, corporate income tax and business credits and rebates.

Dr. McDonald, chair
Representative Arnold-Jones
Ms. Haynie
Senator Smith
Representative Taylor
Mr. Sandel (ex officio)

Equity Committee. This committee assessed exemptions and deductions in all programs, but concentrated on gross receipts taxes, dissimilar treatment of taxpayers in similar situations, compensating tax, special state gross receipts taxes and local option gross receipts taxes.

Governor Carruthers, chair
Senator Aragon
Representative Harrison
Ms. Hays
Mr. King
Mr. Martinez
Mr. Sandel (ex officio)

Family Committee. This committee examined the personal income tax, the application of gross receipts tax to receipts from sales of food and the taxation of medical practitioners and nursing homes.

Senator Leavell, chair
Mr. Fulginiti
Senator McSorley
Mr. Morgan
Mr. Nathan
Senator Rawson
Mr. Sandel (ex officio)

Selective Excise Tax Committee. This committee looked into highway revenues, the motor vehicle excise tax and other excise taxes and fees.

Mr. Becker, chair
Speaker Lujan
Mr. Ryan
Governor Sanchez
Representative Whitaker
Mr. Sandel (ex officio)

d. Public Outreach

The commission believed open communications channels were an essential element of the process, that they were necessary for explaining issues, sorting through alternative solutions and reaching genuine consensus.

Thus, continuous contact with the public was important to the commission, especially in view of the compressed time frame. A page was set up on the legislature's web site (www.legis.state.nm.us, with links to other appropriate governmental sites). The commission's schedule, membership, agendas and minutes were posted on this page. More importantly, the reports and documents generated by the commission and its staff, as well as all electronic submissions to the commission, were also posted. Commission staff also listed the paper documents received, by meeting. The names, telephone numbers and email addresses of Jim O'Neill and Janice McCrary were posted to ensure that the public had specific contacts.

The commission held two meetings specifically to gather comments from the general public. The first was at the Farm and Ranch Museum in Las Cruces on August 4, 2003 from 3:00 p.m. to 7:00 p.m. The second was the following day in Albuquerque at Technical-Vocational Institute's Smith-Brasher Hall from 3:00 p.m. to 7:00 p.m. Both of these meetings were devoted solely to receiving comment, opinion and information from the public. (See Appendix C-3.)

Public input was encouraged in other ways. At meetings of the full commission (except the final meeting on October 14) and meetings of the committees, time was reserved for comments from the public. In addition, individuals and groups were scheduled on the agendas to present formal testimony. The public also submitted letters and other documents. All of these are summarized in Appendix C-4.

The commission would like to acknowledge its appreciation for the time, efforts and patience of all those who presented information to the commission, attended commission meetings and responded to the commission's requests for information.

Goals, Objectives and Constraints

The commission's general goal was to align New Mexico's taxes more closely with its economy and its future. Members also hoped to achieve progress with several specific problems.

Many of the specific concerns focused on the single largest source of revenue for the state and its municipalities, the gross receipts tax. It is well known that the gross receipts tax structure permits relatively extensive pyramiding of tax on the performance of services. Further, rules for proving entitlement to the most commonly claimed gross receipts deductions are inflexible, leading to what are referred to as "gotcha" audits. Medical professionals assert that application of gross receipts tax to their receipts under managed care contracts (which do not allow pass-through of tax amounts) is a major reason for the perceived shortage of medical professionals in the state. The commission was also concerned with whether the regressivity of the tax system (and the gross receipts tax in particular) would be best blunted by exempting sales of food or by other approaches.

Issues arose in other revenue programs as well, for example:

- The wide menu of choices built into the corporate income tax could be taken as an economic development incentive or as an unnecessary leakage of revenue.
- The specific charge to the commission was to re-examine the cuts in the personal income tax made earlier in the year.
- Administration of the tax laws was another topic of interest, particularly in continuing and refining efforts to build more flexibility and eliminate unnecessary rigor in the laws by which the Taxation and Revenue Department administers the taxes.

Finally, serious concerns were expressed about the inadequacy of funding for our highways. A good road system is thought to be one of the keys to successful economic development. There are those who argue that the backlog of repair, re-design and improvement work on New Mexico's highways is unacceptably high. One reason cited is the lack of adequate funding over the last several years, and this inadequacy is projected to persist into the future unless the revenue system is changed.

The commission resolved to tackle these problems through an analysis based on tax principles. The principles of a good tax system have a venerable pedigree, tracing back to Adam Smith and even earlier writers. The reason for looking to these principles is simple: tax systems developed on principles tend to stand the test of time. They require less adjusting and are generally perceived as fairer. New Mexico's present arrangement, which has served the state over 30 years, arose from a series of principled examinations during the 1960s and early 1970s.

Adequacy is a cardinal principle of taxation; taxes that do not raise the required revenues are failures no matter how fair or easy to administer they may be. Determining what revenue is required to finance government is the quintessential question of government. The commission

recognized that even attempting to frame a general answer as to adequacy lay well beyond its mandate, except where a solid case could be laid before it on a specific program. The commission took its mission as reform rather than adjusting the total tax burden substantially. Reform of a tax system does not imply that the end result will either raise or reduce revenues in the short run. It could be that, by making taxes more closely fit the economy's structure and the community's preferences, more revenues will be produced over time with less friction, more feathers plucked with fewer squawks from the goose.

Fixing problems does require resources, and resources are limited. The New Mexico Constitution (Article IX, Section 7) implies that the state's budget must be balanced. Tax changes can affect state and local budget balances. Therefore, a concern for the fiscal health of the state and local governments, both currently and over the forecast period, influenced the commission's deliberations. Good fiscal health provides more scope for reform, while ill health creates more need.

New Mexico is just one of 50 states. It shares a border with one of this country's NAFTA partners. Modern telecommunications ties all these jurisdictions more tightly together every day. All these jurisdictions compete for private sector jobs and income because these jobs create the economic foundation. What other states, especially neighboring states, do with their taxes can affect private businesses' decisions in New Mexico or influence their decisions to locate in New Mexico. The commission, therefore, had to be cognizant of the effect of proposals on New Mexico's competitive position vis-à-vis other states.

National and international events and trends impinge upon New Mexico and must be factored into the design of any state or local tax plan. The dependence of the New Mexico economy on the price of minerals, particularly oil and natural gas, and the size and type of federal spending in this state are bedrock facts of our economic landscape. New Mexico's tax system is partially linked to the federal system. Federal downsizing of the personal income tax base and the elimination of the estate tax invoked mirroring responses from the state's taxes. The movement toward a standardized sales tax can be ignored only at New Mexico's peril. The present national anti-tax mood certainly constrains available options.

The commission realized that some taxes are less unpopular than others. Thus, some options, however appealing on a more theoretical basis and however acceptable in other states, simply were not viable alternatives here. The relative burden of property tax in New Mexico has been one of the very lowest among the states for decades. New Mexico's history and the thicket of property tax provisions in the state constitution, however, dissuade most potential reformers from attempting to suggest any meaningful restructuring of this tax. There is considerably more flexibility in dealing with other revenue sources, few of which are even mentioned in the constitution. The law creating the commission ensured that its deliberations would be sensitive to the practical business of getting its recommendations through the political process by requiring approval of a majority of the 10 legislative members.

The commission's main constraint was the time allotted to it. Originally, it was granted a little over five months from the last few days of April to September 30. The subsequent extensions, while short, did allow enough time for the commission to complete its work. The principled approach helped the commission make the best use of its time. Some revenues, such as the sin taxes, are parts, and often minor parts, of debates on larger issues of social policy. Most commission members preferred to leave debate and resolution of such issues to the most appropriate forum, the legislature.

The commission also faced the reality that tax restructuring had started before the commission was launched. In the 2003 regular session, a significant cut in personal income tax rates and capital gains taxation was enacted, phased in over five years, creating a potential fiscal hole of some magnitude for the 2007 and subsequent fiscal years. The governor also made clear that any serious alteration of this tax cut would not be tolerated.

Key Issues

The commission considered the following key issues in formulating its recommendations.

a. Tax Relief for Low- and Middle-Income Families. The commission spent much time considering the need for tax relief for low- and middle-income families, including various proposals to eliminate or reduce the gross receipts tax on food and various proposals to provide relief through the income tax system. The food tax proposals, while simple in theory, got bogged down by the impact on local governments and whether they should be held harmless from the significant impact of the food tax on their revenues.

Proponents of repealing the food tax believe that it is regressive and wrong to tax necessities such as food, and believe that approximately 90 percent of the benefit would go to working low- and middle-income families. Additionally, proponents point out that New Mexico is one of only eight states to fully tax food.

Opponents of repealing the food tax believe that a significant number of low-income households that participate in the federal food stamp program would not benefit at all from removing the gross receipts tax, since food purchased using food stamps is already exempt from the tax. Opponents cite data showing that higher-income families would receive most of the actual benefits in terms of total dollars and believe that the relatively high cost of the removal of the tax could be reduced by providing a tax rebate, administered through the income tax program, targeted at low- and middle-income families. They also noted the administrative burden on the Taxation and Revenue Department of administering a food exemption, especially with a hold harmless provision for local governments.

In the end, the commission voted to retain the current tax treatment of food, but to provide targeted tax relief to low- and middle-income families roughly equivalent to their food tax burden through the state income tax. The proposal adopted by the commission would provide \$45 million in tax relief to about 500,000 families and individuals by raising the low-income comprehensive tax rebate (LICTR) and increasing the personal exemption allowance. In addition to addressing the food tax burden, this proposal was structured to provide tax relief to those New Mexicans who did not benefit from the income tax cuts approved earlier in 2003. The reduction averages about \$85.00 per tax return. Since the amount is tied to the number of exemptions, however, families with children receive more than those without. The benefits are split about equally between taxpayers who qualify for LICTR, who generally do not have an income tax liability, and taxpayers with somewhat higher incomes (up to \$48,000 of adjusted gross income), who do have a tax liability.

The commission also approved a proposal to help the approximately 78,000 single-parent families who currently pay higher income taxes than two-parent families at the same income level. An additional \$2.4 million of relief was proposed for those filing as head of households by giving them parity with married filing joint tax rates.

b. Services of Medical Practitioners. Good medical service is not only a necessity for the state's communities, it also has an economic development component. Poor or nonexistent medical service can induce a firm to strike a locality from its list of potential sites. It has become common wisdom that New Mexico is underserved with medical practitioners. The extent and cause are matters of debate. One argument is that the gross receipts tax imposed on medical services helps drive practitioners away or deters them from moving to New Mexico. Medicare and most, if not all, private managed care plans do not specifically reimburse practitioners for the cost of the gross receipts tax. Hence, the practitioner bears the tax in the form of lowered net income from the practice. While a six percent tax on gross revenues may not seem burdensome, testimony was presented that it can represent 25 percent or more of the practitioner's net income, using national averages. It could even exceed the practitioner's federal income tax liability.

The commission determined that although the best way to resolve this issue would be to require Medicare and private managed care plans to add a reimbursement for gross receipts tax to what is paid to the practitioners, the state has no power to mandate gross receipts tax reimbursement for Medicare. Further, numerous contractual and practical issues preclude requiring it of private plans.

Accordingly, the commission recommended a deduction for practitioner receipts from Medicare Part C and private managed care plans. For the medical services not provided through managed care regimes but paid under more traditional insurance plans or even on a cash basis, there is no contractual bar to the practitioner including tax on these billings.

c. Gross Receipts of Hospitals. For years, the tax system has treated the several types of hospitals disparately. The receipts of government hospitals and 501(c)(3) hospitals are exempt from gross receipts tax. Hospitals organized as health maintenance organizations (HMOs) pay a three percent premiums tax instead of the gross receipts tax. Non-HMO for-profit hospitals are subject to the gross receipts tax but with a 50 percent deduction. The commission noted that federal law prohibits hospitals from turning away patients, so many of the services provided by the several types of hospitals are much the same. This suggests that the tax system should treat them similarly.

One alternative would be to tax all hospitals at the full gross receipts tax rate. Testimony indicated this would impose hardships and possibly force service cuts on at least some of the nonprofits and might impose a need for higher taxpayer support of governmental hospitals. Since private hospitals are in the distinct numerical minority, the commission decided to recommend that non-HMO hospitals be granted a 100 percent deduction to give them equivalent tax treatment with governmental and nonprofit hospitals.

d. Tax Treatment of Commercially Active Nonprofits. Nonprofit organizations designated as 501(c)(3) or in some cases as 501(c)(6) organizations by the Internal Revenue Service are exempt from gross receipts tax. Under the principle that people in similar situations ought to be

taxed similarly, the commission, particularly its Equity Committee, investigated imposing gross receipts on nonprofits that could be viewed as competing with for-profit and taxed businesses.

The most noted example is the situation in which one national laboratory is fully taxable and the other is exempt. In the end, the commission simply did not have enough time to explore this complicated area in the required depth. No scheme to separate out the commercially active by size of revenues was workable. Accordingly, it made no recommendation in this area, except to require some of the larger nonprofits to report receipts and deductions. It observed, however, that some other states do not automatically adopt the determinations of the Internal Revenue Service, but make their own.

e. Personal Income Tax Rates and Capital Gains. The commission was charged specifically with reviewing the phased-in income tax cut passed earlier in the year. It did so. Some consideration was given to smoothing the steps of the phase-in, as well as to delaying or suspending some of the later rate reduction steps. This would have resulted in the same end-level of tax but would have softened the fiscal impact in the third and fourth years. Whether the rates are too high or low concerns adequacy of revenue. The commission took a neutral position for the general revenue portion of its recommendations and, so, did not pursue changes to the phase-in pattern.

Treatment of capital gains is more than an issue of adequacy. Vertical equity considerations are also involved. The personal income tax rate cuts combined with the expanded exemption of capital gains flattened the effective rate curve of the New Mexico tax. Since the personal income tax is the major progressive element in the state's tax system, the cuts produced a more regressive overall tax structure. To restore some of the progressivity, the commission recommended capping the new capital gains benefits. To retain at least some of the economic development boon that the expanded capital gains deduction was to produce, the commission also recommended allowing a full exemption for capital gains from selling closely held New Mexico businesses.

f. State Road Fund Sources. The secretary of transportation made a convincing case that New Mexico was not devoting enough resources to its highway system. Accordingly, the commission recommended increasing a number of revenue sources that support the State Road Fund. In particular, the commission recommended increasing the gasoline and special fuel tax rates. Some trepidation was expressed that increasing these taxes involves high political risk, citing the fact that Governor Johnson rode to office opposing a six-cent hike in these taxes. The commission felt that this fear was misdirected since popular opposition was aimed more at the diversion of the revenues to the General Fund than to the fact of the increase. In addition, tourists and commercial vehicles passing through the state pay part of the fuel taxes, whereas some alternatives, such as increases in driver's license fees, are borne almost entirely by New Mexicans.

g. Liquor Taxes. New Mexico has a very serious problem with abuse of alcohol. It is always near the top in state rankings on driving while intoxicated. One suggested way to combat this is to make alcohol more expensive, thereby, hopefully, reducing the quantity demanded. Simultaneously, the additional revenues could fund programs to combat the problem and its aftermath.

The commission agreed that all New Mexicans must continue to attack this problem and that taxation plays a part. However, many members of the commission expressed the opinion that dealing with alcohol abuse is a much larger issue than the liquor excise tax, and is more appropriately addressed by the legislature and the governor.

h. Corporate Income Tax. In New Mexico and around the nation, corporate income tax receipts have been declining relative to corporate profits for 10 years or more. Because this is a very complex tax, more than one cause exists for the drop-off. The one that is often pointed to, however, is the increasingly sophisticated use by corporate tax planners of differences in state laws and the lack of communication among states that allows corporations to shelter income from taxation. New Mexico allows corporations in corporate groups to file income tax reports under three different methods. Obviously, corporate groups will choose the reporting option that minimizes tax liability. Originally, this menu of choices was promoted as an economic development incentive.

The commission also recognized that the lower personal income tax rates give competing forms of business organization, such as limited liability companies, a tax advantage over regular corporations. Absent corrective action, New Mexico could expect revenues from corporations to continue declining relatively.

Often touted as the fairest approach to corporate taxation at the state level, reporting as a combined unitary business eliminates much of the game playing. It does require the tax agency to take an active role in determining which elements of a corporate family are "unitary". As a matter of equity, the commission noted that a business operating solely in New Mexico does not have the same opportunities to shift income to lower tax jurisdictions as a competitor that is a member of a multistate corporate family. Because fairness is the issue and because there really is no rationale for a step-rate corporate income tax, the commission also recommended an offsetting reduction in the corporate income tax rate structure. The rate decreases were phased in to match changes in the personal income tax rates. The commission recommended that these changes not begin prior to the 2005 tax year in order to give the Taxation and Revenue Department and the companies time to prepare for the new filing method.

Summary of Recommendations

The commission formally developed 196 separate proposals to alter the tax system. (See Appendix B-1 for a complete listing.) A number of additional ideas were raised but did not garner enough support to become formal proposals.

The commission adopted 71 specific recommendations; a brief description of each follows. The fiscal impacts of those recommendations are laid out in the table below beginning on page 26. A more detailed description of each item and arguments for and against the option are presented in Appendices A-2 through A-10. Legislative text of each option is included in Appendix D.

The recommendations fall into two groups. The first group deals with general revenues available to state and local governments. The commission's general intent was that this group of proposals address specific issues in the tax system and that, overall, the revenue impact of the recommendations be approximately revenue neutral. The second group comprises a transportation funding package and it was the commission's intent that these total revenues be increased significantly.

a. Studies Recommended. The commission recommended two further studies be undertaken.

- A study should be undertaken to establish a process under which all economic development incentives would be evaluated regularly for effectiveness and achieving their stated goals. Persons taking advantage of each incentive would be required to agree to provide necessary data relevant to the evaluation. An annual report would be submitted to the legislature. Without this data, the state will have difficulty finding out which approaches are the most effective.

- The Revenue Stabilization and Tax Policy Committee or another suitable body should conduct an in-depth examination of the administrative side of the Property Tax Code. The code was created in the early 1970s. The administrative provisions reflect the technological and information-processing capabilities prevailing over 30 years ago. Those provisions have not been systematically reviewed or upgraded in that interval. Taking advantage of current information technology and statistical methodology can refocus the code away from spelling out procedure to a concentration on proper valuation, a genuine two-pronged protest option, instilling accountability and making more accessible the vast amounts of information locked up in that tax system. The commission also recommended as part of this study an examination of property tax equity issues, such as whether government properties used commercially should be subject to tax.

b. Description of Recommendations. Brief descriptions of each of the commission's specific recommendations are listed below.

STREAMLINED SALES TAX:

Participate in the Streamlined Sales Tax Project. This recommendation permits New Mexico to join the organization of states that is implementing the streamlined sales tax agreement and its attendant administrative bodies. The commission found that New Mexico would benefit from joining the agreement as a voting member. Joining the organization does not commit New Mexico to restructuring its taxes but does give it a voice in the design of the standardized system.

FAMILY:

Providing Additional Income Tax Relief to Families and Restoring Progressivity of the Income Tax:

Expand LICTR using FAIR concepts and increase personal exemption amounts. This expands the low-income comprehensive tax rebate (LICTR), adding a column for family sizes of seven exemptions and renaming it as the family and individual rebate (FAIR). The rebate amounts are updated to more realistic levels. The value of food stamps received by a LICTR claimant is added to the definition of modified gross income to more fairly measure real income. Also, this recommendation grants a new exemption up to \$3,000 for low-income and middle-income taxpayers to ensure that they share in the income tax cuts.

Phase out capital gains deduction for high-income taxpayers. Part of the commission's charge was to review the income tax reduction enacted earlier this year. The commission recommended mitigating the future fiscal impact of the income tax reductions and restoring some progressivity by trimming the capital gains deduction.

Provide capital gains deduction for sales of closely held businesses. Another recommendation proposes to exclude the entire gain from the sale of closely held New Mexico businesses. This provides an incentive for investing in New Mexico and keeps the money in-state for reinvestment.

Consolidate filing status to two categories. This recommendation provides \$2.4 million in tax relief for single-parent families who pay higher income taxes than two-parent families at the same income level.

MEDICAL SERVICES:

Reducing, Eliminating or Compensating for the Gross Receipts Tax on Health Care Practitioners:

Deduction for all practitioners for reimbursements from commercial managed care and Medicare "C". The commission formulated this recommendation in response to the suggestions of medical professionals who expressed concern regarding their inability to pass on the gross receipts tax. By eliminating the gross receipts tax on commercial managed care contracts and on Part C Medicare, the concerns of those medical professionals can be partially alleviated. Since the availability of adequate medical services is conducive to economic development, local governments are asked to share the cost of this proposal.

ECONOMIC DEVELOPMENT:

Gross Receipts Tax Pyramiding:

Repeal the "next sale taxable" requirement of Section 7-9-48 NMSA 1978 except for sales to governments and nonprofits. Businesses have long suffered the undesirable effects of pyramiding with respect to the taxation of services. This recommendation strikes the "next sale taxable" requirement, except for sales to governments or nonprofits, which should diminish the effects of tax pyramiding.

Corporate Income Tax:

Establish a two-tier corporate income tax rate with a top rate of 6.4 percent. The existing three-tier corporate income tax table is converted to a two-tier table with a top rate of 6.4 percent by tax year 2005. The rate reductions are intended to match the personal income tax rate reductions.

Require corporations to use unitary filing method. Affiliated corporations may currently report income using one of three methods. Beginning in 2005, this recommendation requires corporations to use the unitary filing method. The delayed effective date would allow the Taxation and Revenue Department and corporations time to adjust to the change.

Decouple from federal bonus expensing provisions. Most income tax states have decoupled from the recently extended federal "bonus" depreciation provisions. Although the federal government intends this as a stimulus for the national economy, its only certain effect might be to reduce state revenues now in exchange for a possible gain in future years. The commission thus recommended decoupling from the federal

provisions.

Economic Development Incentives:

Require a study of economic development incentives. The commission recommends directing a study of all economic development tax incentives to determine whether those incentives should be retained or expanded.

Provide a high-wage tax credit. This recommendation involves the adoption of a tax credit to reward New Mexico businesses that create high-paying jobs in this state. The credit applies against gross receipts, compensating and withholding taxes and is refundable.

One-time motor vehicle excise tax exemption for purchase of clean, fuel-efficient vehicles. This recommendation would exempt new alternative fuel and gas-electric hybrid vehicles from the motor vehicle excise tax. It is a one-time exemption, available only when the original certificate of title in New Mexico is issued.

Provide a "tax holiday" for small high-tech research businesses. The commission recommends a three-year tax holiday from gross receipts and compensating taxes for small research and development start-up companies. Small companies include those that employ 25 or fewer employees and have less than \$10 million in receipts. Government-funded research would not be eligible for the tax holiday.

Franchise Tax:

Increase the franchise tax from \$50.00 to \$100. The \$50.00 franchise tax on corporations has not been adjusted since the 1980s. This recommendation increases the tax to \$100.

Impose the franchise tax on limited liability companies (LLCs) and other flow-through entities at \$100. LLCs and limited partnerships enjoy many of the same limited liability benefits as corporations. Imposing the same tax on LLCs and limited partnerships would promote fairness.

Increase the annual filing fee for corporations and nonprofits to \$100. The fee associated with the filing of the corporate annual report with the Public Regulation Commission would be equalized at \$100 for nonprofits (up from \$10.00) and for-profits (up from \$25.00).

Administrative Reforms:

Implement an independent hearing process. This is the most significant of the several administrative reform proposals. To respond to the perception of a lack of independence in the current hearing process, the commission recommended removing the Taxation and Revenue Department's hearing officers and making them administrative law judges in a separate agency attached to the General Services Department. These judges would continue to hear tax protests but would not be supervised by the Taxation and Revenue Department.

Raise the minimum amount of tax for which an assessment may be issued from \$10.00 to \$25.00. The Taxation and Revenue Department must assess when a taxpayer is \$10.00 or more in arrears. This is administratively inefficient, creating a great amount of paperwork and requiring the inefficient use of manpower. A new floor of \$25.00 is proposed.

Taxpayer election to use rules of civil procedure. The hearings before the Taxation and Revenue Department's hearing officers are run by a set of internal procedures that are more relaxed than those of the district courts. Some taxpayers believe the hearings should be conducted utilizing more formal district court procedure, particularly in complex cases.

Provide for protective claims. The Taxation and Revenue Department allows taxpayers to file protective claims. These are claims filed on the same or similar basis used for a claim by another taxpayer in another action. These claims are allowed to pend the resolution of the lead case. This recommendation would provide a formal provision for such claims.

Modify interest paid on deficiencies and overpayments. This recommendation would lower the interest rates paid by or to the Taxation and Revenue Department. The current annual rate is 15 percent. The proposed rate would be 10 percent initially and then, beginning January 1, 2006, would equal and float with the Internal Revenue Service (IRS) underpayment rate. The IRS rate is adjusted quarterly based on market rates.

Raise the minimum penalty for failing to file from \$5.00 to \$25.00. This recommendation proposes an increase in the penalty for failing to file. The \$5.00 penalty for late filing has not been changed in decades and does not provide much of an incentive to file timely.

Allow taxpayers to request regulations. This recommendation provides a formal mechanism by which taxpayers can ask for regulations or modification of existing regulations.

Extend or eliminate nontaxable transaction certificate (NTTC) conversion deadline.

The streamlined sales tax agreement mandates that its member states use only one tax certificate form. New Mexico has well over a dozen types of certificates in use presently. The Gross Receipts and Compensating Tax Act requires the Taxation and Revenue Department to swap out its existing series for a new one by the end of 2004. A conversion will cost several million dollars, an effort that will be futile if New Mexico joins the streamlined sales tax agreement in the near future.

EQUITY:

Gross Receipts and Compensating Tax Issues:

Reporting requirements for certain nonprofits — convert the exemption for 501(c)(3) and (c)(6) organizations, excluding churches, with receipts in excess of \$250,000 (adjusted for inflation annually) to a deduction. One difficulty the commission was not able to overcome to its satisfaction was the lack of data on the market presence of nonprofit organizations. This recommendation would convert the existing exemption (which requires no reporting) to a deduction (which does require reporting). This would apply to nonprofit organizations with \$250,000 or more in receipts.

Expand Section 7-9-71.1 NMSA 1978 deduction for for-profit hospitals from 50 percent to 100 percent. Under current law, for-profit hospitals may deduct 50 percent of their gross receipts. This recommendation would allow them to deduct 100 percent of gross receipts, putting them in parity with the governmental and nonprofit hospitals.

Tax employee leasing like temporary services. The tax obligations incurred when operating two very similar services should be treated the same.

Tax bail bondsmen under gross receipts tax rather than insurance premiums tax. The argument was made that bail bondsmen provide a service rather than the sale of insurance and should be taxed as other sales and services are taxed.

Repeal Section 7-9-54.1 NMSA 1978 deduction for research and development sales to one specific aerospace corporation. The aerospace corporation is a nonprofit 501(c)(3) that buys for the United States Air Force's Phillips Laboratory. It is located primarily in California. This deduction was offered as an incentive for this business to locate in New Mexico, which it never did. Further, no other part of the armed forces enjoys this treatment. The commission's recommendation was to remove this deduction.

Convert Section 7-9-55 NMSA 1978 to a "delivery rule". New Mexico's rule on whether exports of tangible property are deductible is out of step with the majority of other states. Generally, the current requirement is that the product be delivered out of state to the buyer prior to use. New Mexico also requires that risk of loss and title pass out of state. This recommendation would drop those requirements and align New Mexico's rule with other states.

Put agricultural implements, aircraft and vehicles not required to be registered under the Motor Vehicle Code under the motor vehicle excise tax. The Equity Committee noted that vehicles are taxed in a variety of ways and at different rates. To put like items under similar tax burdens, several categories of vehicles (agricultural implements, snowmobiles, off-road vehicles, aircraft not required to be registered and motor vehicles not required to be registered under the Motor Vehicle Code) are removed from the gross receipts tax and placed under the motor vehicle excise tax.

Repeal deduction for newspapers. Whether newspaper sales are regarded as sales of tangible personal property or the provision of an information service, equity would dictate that those sales be treated like sales of closely related products, such as magazines and books.

Eliminate deduction in Section 7-9-65 NMSA 1978 for sales of chemicals and reagents in excess of 18 tons sold to unspecified entities. A deduction for sales of chemicals and reagents sold in carload lots is eliminated. Sales for resale and use of chemicals and reagents in mines, wells, refineries, etc., are deductible under other provisions.

Repeal Section 7-9-70 NMSA 1978 deduction for leasing vehicles used in interstate commerce. Section 7-9-70 NMSA 1978 provides a deduction for vehicles used in interstate commerce by taxpayers subject to regulation by the Interstate Commerce Commission (ICC). The ICC was abolished years ago. The commission's recommendation is to repeal this outdated deduction.

Remove the \$5,000 limit in Section 7-9-74 NMSA 1978 for property used in the manufacture of jewelry. Currently, there is a \$5,000 limit on the sales of inputs to Native American jewelry makers. These Native American businesses may not be required to register for gross receipts tax purposes and, therefore, do not qualify for nontaxable transaction certificates. There is no logical reason for the limit and, should New Mexico decide to pursue the streamlined sales tax agreement, such limits would be barred by the streamlined sales tax agreement.

Apply gross receipts tax to rental of storage units. In most cases, rental of storage units can be viewed as the rent or lease of real property, which is deductible under gross receipts tax, or the grant of a license for the use of the property, which is taxable. This recommendation removes receipts from rental storage units from the deduction for rental of real property, and clarifies that rental of storage units is the granting of a license for the use of the property.

Reduce municipal gross receipts tax credit (reflects .125 percent reduction); increase municipal distribution to 1.25 percent. The state gives a taxpayer credit for 0.5 percent of the municipal gross receipts tax imposed by the taxpayer's municipality. The effect is that the state's five percent gross receipts tax rate is cut to 4.5 percent for transactions within municipalities, but the rate is not cut for counties. This recommendation reduces the amount of the credit, which raises general fund revenues and, effectively, increases the total gross receipts tax facing the taxpayer.

Impose local option compensating taxes. Municipalities and counties have been permitted to impose local option gross receipts taxes for decades but have not been allowed to levy the matching compensating tax. The argument for state-level compensating tax is equally compelling for local option compensating tax. If New Mexico should join the streamlined sales tax agreement, revenues due New Mexico by out-of-state vendors will depend on total compensating tax due, not gross receipts tax.

Apply compensating tax to all imported services. Current compensating tax law applies only to the imports of tangible personal property. This recommendation would extend compensating tax to imported services to more closely resemble the base for gross receipts tax.

Impose compensating tax on certain on-reservation purchases. Manufactured homes are being sold on-reservation by tribal members to non-tribal members for use off-reservation. This recommendation would make these transactions subject to compensating tax just as if the product were imported from another state. Transactions subject to a tribal gross receipts tax administered by the Taxation and Revenue Department would not be affected.

Other State-Imposed Gross Receipts Taxes:

Expand governmental gross receipts tax base to include receipts from parking, airport fees, marina fees, etc. This option expands the list of items subject to governmental gross receipts tax to include parking, airport tie-down fees and other similar kinds of activities.

Raise the interstate telecommunications gross receipts tax rate to five percent.

This recommendation is based on the equity principle and increases the interstate telecommunications gross receipts tax rate from 4.25 percent to five percent to match the rate for gross receipts tax.

Increase leased vehicle gross receipts tax surcharge by \$2.00 per day to \$4.00. The additional revenues would mainly offset negative impacts of other recommendations.

PROPERTY TAX:

Study Property Tax Code administrative provisions and other issues, including ad valorem taxes on state land. The Property Tax Code was written and adopted in the early 1970s. Technology and administrative techniques have advanced since then, offering opportunities to improve the administration of the property tax system.

Enact property transfer tax on residential re-sales with graduated rates of one percent to two percent on amounts over \$100,000. New Mexico's reliance on property tax is relatively light. This recommendation would increase revenues from resales of property, partially redressing the fiscal imbalance with income taxes and sales taxes.

SELECTIVE EXCISE TAXES:

Motor Vehicle Excise Tax:

Raise rate to 4.5 percent, phased in over two years, with .5 percent to State Road Fund. This recommendation increases the motor vehicle excise tax rate to four percent on July 1 and to 4.5 percent a year later. The new rate would move the excise tax rate to more closely resemble the five percent rate on most commodities. The final increase of .5 percent would go to the State Road Fund.

Establish default value for sales of used vehicles (at 4.5 percent with .5 percent to State Road Fund). The commission concluded that many private sales prices of motor vehicles are understated. This recommendation presents a standard of value to be used in resale transaction. The value would be based on the blue book value of the basic vehicle with exceptions for salvage vehicles and inter-family transfers.

Cigarette Tax:

Capture tax on sales of tobacco to non-Indians on tribal land following government-to-government negotiations. This recommendation would make continuation of the exemption for sales to tribal smokeshops contingent upon a negotiated agreement between the tribal government and the state and could rectify a competitive disadvantage of non-tribal vendors.

Combine distributions to local governments. The recommendation combines two small distributions of cigarette revenues by the state to local governments. The primary purpose is to cut administrative expenses.

Eliminate discount for stamping. The discount for stamping arose primarily from the laborious task of manually affixing cigarette tax stamps to cigarette packages. No other tax program reimburses vendors for the cost of complying with the tax program.

Tobacco Products Tax:

Raise rate from 25 percent to 45 percent. The rate of the tobacco products tax on cigars, smokeless tobacco and pipe tobacco is currently less than that charged on cigarettes. This recommendation would realign the level of taxation of the two products since the \$.70 increase on cigarettes enacted in 2003.

Insurance Premiums Tax:

Subject third-party administrators to gross receipts tax. Under current law, receipts of an insurance company are exempt from gross receipts tax because insurance premiums taxes are paid on income generated from premiums. Receipts of an insurance company for administering self-insurance plans for other businesses are not taxed under the insurance premiums tax, nor are they subject to the gross receipts tax, unlike those of their non-insurer competitors. This recommendation would subject the income derived from third-party administration to gross receipts taxation regardless of the type of company performing the service.

Implement a pilot project to enhance Insurance Division funding. This recommendation is based on the adequacy of current funding to provide necessary government services in administering the complex laws surrounding the insurance industry. It provides for a pilot project to provide funding from the pool of revenues collected by the Insurance Division.

Pari-Mutuel Tax:

Eliminate economic development credit; earmark 50 percent of receipts to state fair for capital improvements, except for casino and racetrack. This recommendation would eliminate the credit granted by the pari-mutuel tax to racetracks equal to the amount the track spends on capital improvements or advertising. Roughly half of the increased revenues to the state are earmarked instead for capital improvements at the state fairgrounds (except for the casino and racetrack facilities). If the track has borrowed money to put the improvements in and pledged the credit in repayment, the

credit will continue for that track until the debt is discharged.

Expand track hours. The recommendation allows racetrack gaming operators to operate their gaming machines 16 hours per day instead of 12. By increasing the hours, racetrack operators will have two shifts eligible for full-time benefits. This should also enhance the tracks as tourist attractions.

Boxing and Wrestling Taxes:

Change to fee and authorize agreements with tribal governments. The New Mexico Athletic Commission collects two "privilege" taxes on the conduct of live boxing and wrestling matches in New Mexico and on closed-circuit or other video presentations of such bouts in New Mexico. Currently, most live bouts in the state take place at tribal venues. Although the commission does not have jurisdiction, it is usually invited to supervise these events for a fee. This proposal is to convert the taxes to fees and allow the commission to negotiate a fee for its services when the venue is on tribal territory.

Exempt receipts from gross receipts tax. Since boxing and wrestling matches are already subject to tax by the two privilege taxes, imposition of the gross receipts tax is seen as an impediment to bringing these types of events to the state and puts private venues at an unfair competitive disadvantage to tribal venues. This recommendation proposes to exempt receipts from events subject to the privilege fees from gross receipts tax.

Oil and Gas Emergency School Tax:

Increase tax rate on oil to four percent from 3.15 percent. Under the oil and gas emergency school tax, the rate imposed on oil is 3.15 percent. The rate on natural gas is four percent. There is no rate disparity in any of the other oil and gas taxes. The commission recommends resolving this disparity by changing the rate on oil to four percent.

Other Taxes:

Enact 33 percent tax of collected punitive damages, after attorney fees and expenses, with receipts earmarked into a public trust fund. Punitive damages are a penalty, a sanction imposed by the public against some form of objectionable behavior. Even though a private party may initiate the process by which these damages are awarded, the commission decided that this is not a sufficient reason for enriching the private party. Under this recommendation, the cost to the private party of initiating the process would be fully reimbursed and part of the penalty would be transferred to the state.

TRANSPORTATION FUNDING:

Gasoline Tax:

Increase by two cents immediately. This recommendation is based on the adequacy of funding available to maintain the highway infrastructure of the state. Current funding has been eroded by inflation and lack of rate adjustment since 1995.

Index tax, impose a one-cent-per-year limit. This recommendation permits the gasoline tax rate to be tied to an index that measures inflation. Increases could not be more than one cent per year.

Special Fuel Tax:

Increase by three cents immediately. This recommendation is based on the adequacy of funding available to maintain the highway infrastructure of the state. Current funding has been eroded by inflation and lack of rate adjustment since 1995.

Index tax rate; impose a one-cent-per-year limit. This recommendation permits the gasoline tax rate to be tied to an index that measures inflation. Increases could not be more than one cent per year.

Weight Distance Tax:

Improve administration of weight distance tax and charge an administration fee. The commission's recommendation instructs the Taxation and Revenue Department to improve its administration of the weight distance tax and authorizes it to charge and retain a fee for each identifying certificate issued sufficient to defray costs of administration. The fee should not exceed \$10.00 per card.

Increase rate by 26.26 percent. Since heavy trucks cause more wear and tear on the highways than other vehicles, this recommendation allows those vehicles to bear a larger share of the burden of maintaining the highway infrastructure.

Oversize/Overweight Permits:

Increase fixed fees to equal liquid hauler fee. Oversize and overweight fees are arguably too low given the costs these users inflict on the highways. This recommendation recognizes that there has been no rate structure maintenance in over two decades and the inconsistent charges between types of haulers. This recommendation proposes increasing permit fees to \$35.00 per trip and annual permits to \$120.

Impose additional ton-mile fee for overweight. The commission recognized the inequity in assessing a single fee without regard to the weight of the user. This recommendation assesses an additional fee of one cent for each 2,000 pounds of excess weight times each mile traveled in New Mexico. Excess weight is weight over the 86,400 pound maximum.

Vehicle Registration Fees:

Increase by an average of \$12.50 per year. This option raises vehicle registration fees by an average of \$12.50 per year and is based on the recognition of the erosion of the dollar through inflation.

COUNTY LOCAL OPTION TAX REORGANIZATION:

Consolidate various options and authorize new authority. The general idea is to make the county local option gross receipts taxes look more like the municipal taxes. Over time, the number of county local option gross receipts taxes would be reduced as tax authorizations for specific counties are phased out. Some referenda requirements are removed and a new general one-eighth percent tax authorization is added, in part to offset negative impacts on county budgets of other recommendations.

c. Revenue Impact Table. With respect to the table starting on page 26, it should be noted that the table presents estimates of fiscal impacts as if every option were to be in effect for the entire 12-month period of FY 2005, even when it is anticipated that a particular option would be put into place in another time frame. This is to provide an easy way to compare the relative magnitudes of the various options. Fiscal impact reports prepared for a bill that might embody an option may show fiscal impacts differing from those displayed in the table, depending on the actual effective date proposed in the bill.

**BLUE RIBBON TAX REFORM COMMISSION
REVENUE IMPACT TABLE
OPTIONS ADOPTED BY THE COMMISSION**

		FY 2005 Full-Year Impacts in Millions of Dollars						
		General Fund	Road Fund			Other State Funds	Local Revenue	Total Revenue
			1st Phase	2nd Phase	3rd Phase			
	STREAMLINED SALES TAX							
1	Participate in streamlined sales tax initiative	NI					NI	NI
	FAMILY							
	Providing Additional Income Tax Relief to Families and Restoring Progressivity of the Income Tax							
2	Increase LICTR using some of the FAIR concepts and provide an increase in personal exemption amounts for certain taxpayers; add food stamps to definition of modified gross income	(45.0)						(45.0)
3	Phase out capital gains deduction for high-income taxpayers	17.0						17.0
4	Provide capital gains deduction for sales of closely held businesses	(3.0)						(3.0)
5	Consolidate filing status to two categories - benefits heads of households who would be combined w/ married filing joint	(2.4)						(2.4)
	MEDICAL SERVICES							
	Reducing, Eliminating or Compensating for the Gross Receipts Tax (GRT) on Health Care Practitioners							
6	Deduction for all practitioners for reimbursements from commercial managed care and Medicare "C"--no hold harmless--add a sunset provision	(21.4)					(18.8)	(40.2)
	ECONOMIC DEVELOPMENT							
	Gross Receipts Tax Pyramiding							
7	Repeal the "next sale taxable" requirement of 7-9-48 except for sales to governments and nonprofits	(30.0)					(20.0)	(50.0)
	Corporate Income Tax							
8	Two-tier rate with a top rate of 6.4%	(18.0)						(18.0)
9	Require all corporations to file using the unitary method; use the current NM definition of unitary corporation and nexus (at 6.4%)*	16.0						16.0

**BLUE RIBBON TAX REFORM COMMISSION
REVENUE IMPACT TABLE
OPTIONS ADOPTED BY THE COMMISSION**

		FY 2005 Full-Year Impacts in Millions of Dollars				
		General Fund	Road Fund	Other State Funds	Local Revenue	Total Revenue
	*Effective for 2005 tax year; revenue impact would not occur in FY 2005.					
10	Decouple from federal bonus expensing provisions (at 6.4%)*	6.0				6.0
	*Average revenue over 4 years.					
	Economic Development Incentives					
11	Require a study of all economic development incentives	NI			NI	NI
12	Provide a high-wage jobs tax credit	(1.5)				(1.5)
13	Provide a "tax holiday" for small, high-tech research businesses	(1.0)				(1.0)
14	One-time motor vehicle excise tax exemption for purchase of clean, fuel-efficient vehicles	(0.5)				(0.5)
	Franchise Tax					
15	Increase the franchise tax from \$50 to \$100	2.5				2.5
16	Impose franchise tax on limited liability companies and other flow-through entities at \$100	2.4				2.4
17	Increase annual filing fee for for-profits and nonprofits to \$100	3.0				3.0
	Administrative Reforms					
18	Implement an independent hearing process	NI			NI	NI
19	Raise the minimum amount of tax for which an assessment may be issued from \$10 to \$25	NI			NI	NI
20	Taxpayer election to use rules of civil procedure	NI			NI	NI
21	Provide for protective claims	NI			NI	NI
22	Modify interest paid on deficiencies and overpayments	(4.0)				(4.0)
23	Raise the minimum penalty for failing to file from \$5 to \$25	0.5				0.5
24	Allow taxpayers to request regulations	NI			NI	NI

**BLUE RIBBON TAX REFORM COMMISSION
REVENUE IMPACT TABLE
OPTIONS ADOPTED BY THE COMMISSION**

		FY 2005 Full-Year Impacts in Millions of Dollars				
		General Fund	Road Fund	Other State Funds	Local Revenue	Total Revenue
25	Eliminate nontaxable transaction certificate (NTTC) conversion deadline	NI			NI	NI
26	Eliminate 60-day limit on NTTCs	NI			NI	NI
	EQUITY					
	Gross Receipts Tax & Compensating Tax Issues					
27	Reporting requirement for certain nonprofits - convert the exemption for 501(c)(3) and (c)(6) organizations with receipts in excess of \$250,000 (adjusted for inflation annually) to a deduction, excluding churches	NI			NI	NI
28	Expand 7-9-73.1 deduction for for-profit hospitals from 50% to 100%	(7.0)			(5.0)	(12.0)
29	Tax employee leasing like temporary services	5.0			4.0	9.0
30	Tax bail bondsmen under GRT rather than insurance premiums tax	0.2			0.1	0.3
31	Repeal 7-9-54.1, deduction for R&D sales to one, specific aerospace corporation that did not locate in New Mexico	NI			NI	NI
32	Convert 7-9-55 to a "delivery rule"	(0.1)				(0.1)
33	Put agricultural implements, aircraft and vehicles not required to be registered under the Motor Vehicle Code under the motor vehicle excise tax (4% rate with .5% to road fund)	5.1	1.5		(4.0)	2.6
34	Repeal deduction for newspapers	1.2			0.8	2.0
35	Eliminate deduction in 7-9-65 for sales of chemicals and reagents in excess of 18 tons sold to unspecified entities	0.3			0.2	0.5
36	Repeal 7-9-70 deduction for leasing vehicles used in interstate commerce	0.1				0.1
37	Remove the \$5,000 limit in 7-9-74 for property used in the manufacture of jewelry	(0.1)				(0.1)
38	Apply GRT to rental of storage units	0.8			0.5	1.3

**BLUE RIBBON TAX REFORM COMMISSION
REVENUE IMPACT TABLE
OPTIONS ADOPTED BY THE COMMISSION**

		FY 2005 Full-Year Impacts in Millions of Dollars				
		General Fund	Road Fund	Other State Funds	Local Revenue	Total Revenue
39	Reduce municipal GRT credit (reflects .125% reduction); increase municipal distribution to 1.25%	29.0			7.3	36.3
40	Impose local option compensating taxes	(3.8)			14.1	10.3
41	Apply compensating tax to all imported services	14.5			3.6	18.1
42	Impose compensating tax on certain on-reservation purchases	NA				NA
	OTHER STATE-IMPOSED GROSS RECEIPTS TAXES					
43	Expand governmental gross receipts tax (GGR) base to include receipts from parking, airport fees, marina fees, etc.			5.0		5.0
44	Raise the interstate telecommunications gross receipts tax (ITGRT) to 5%	1.5				1.5
45	Increase leased vehicle GRT surcharge by \$2 per day to \$4	6.6				6.6
	PROPERTY TAX					
46	Study Property Tax Code administrative provisions and other issues, including ad valorem taxes on state land	NI				NI
47	Enact property transfer tax on residential re-sales with graduated rates of 1% to 2% on amounts over \$100,000	12.0			8.0	20.0
	SELECTIVE EXCISE TAXES					
	Motor Vehicle Excise Tax					
48	Raise rate to 4.5%, phased in over 2 years, with .5% to road fund	41.3	20.7			62.0
49	Establish default value for sales of used vehicles (at 4.5% with .5% to road fund)	1.0	0.1			1.1
	Cigarette Tax					
50	Capture tax on sales of tobacco to non-Indians on tribal land following government-to-government negotiations	3.2		1.1	0.2	4.5
51	Combine distributions to local governments				0.0	0.0

**BLUE RIBBON TAX REFORM COMMISSION
REVENUE IMPACT TABLE
OPTIONS ADOPTED BY THE COMMISSION**

		FY 2005 Full-Year Impacts in Millions of Dollars				
		General Fund	Road Fund	Other State Funds	Local Revenue	Total Revenue
52	Eliminate discount for stamping Tobacco Products Tax	1.0		0.3	0.1	1.4
53	Raise rate from 25% to 45% Insurance Premiums Tax	3.0				3.0
54	Subject third-party administrators to GRT	+ ND			+ ND	+ ND
55	Implement a pilot project to enhance Insurance Division funding Pari-mutuel Tax	NA				NA
56	Eliminate economic development credit; earmark 50% of receipts to State Fair for capital improvements, except for casino & racetrack	0.9		0.9		1.8
57	Expand track hours Boxing and Wrestling Taxes	4.2				4.2
58	Change to fee and authorize agreements with tribal govts.	NA				NA
59	Exempt receipts from GRT Oil & Gas Emergency School Tax	(0.7)			(0.5)	(1.2)
60	Increase tax rate on oil to 4% from 3.15% Other Taxes	11.0				11.0
61	Enact 33% tax on collected punitive damages, after attorney fees and expenses, w/ receipts earmarked into a public trust fund TRANSPORTATION FUNDING Gasoline Tax			+ ND		+ ND
62	Increase by 2 cents immediately		16.8			16.8
63	Index tax; impose a 1-cent-per-year limit				8.4	8.4

**BLUE RIBBON TAX REFORM COMMISSION
REVENUE IMPACT TABLE
OPTIONS ADOPTED BY THE COMMISSION**

		FY 2005 Full-Year Impacts in Millions of Dollars					
		General Fund	Road Fund		Other State Funds	Local Revenue	Total Revenue
	Special Fuels Tax						
64	Increase by 3 cents immediately		13.2				13.2
65	Index tax rate; impose a 1-cent-per-year limit			4.4			4.4
	Weight-Distance Tax						
66	Improve cab-card system and charge an administration fee		+ ND		+ ND		+ ND
67	Increase rate by 26.26%		13.8				13.8
	Oversize/Overweight Permits						
68	Increase fixed fees to equal liquid hauler fee		1.3				1.3
69	Impose additional ton-mile fee for overweight		2.0				2.0
	Vehicle Registration Fees						
70	Increase by an average of \$12.50 per year		14.2			7.2	21.4
	COUNTY LOCAL OPTION TAX REORGANIZATION						
71	Consolidate various options and authorize new authority					up to 90.0*	up to 90.0*
						*depends on local decisions	
	Total, General Package (Excluding Road Fund)	50.8			7.3	(2.2)	55.9
	Total, Transportation Package (Road Fund)		61.3	22.3	12.8		96.4

NOTES:

NA: Not enough information on the proposal to enable a fiscal estimate.

ND: Data are not available to permit evaluation.

NI: No fiscal impact.

Revenue amounts provided by the Taxation and Revenue Department and the Department of Transportation. Amounts could change based on specific language in proposed legislation and effective dates.

Final Action

Vote on accepting the amended "Straw Man" of 71 items as the recommendations of the commission:

For

Senator Aragon
Mr. Becker
Governor Carruthers
Mr. Fulginiti
Representative Harrison
Ms. Hays
Mr. King
Senator Leavell
Speaker Lujan
Mr. Martinez
Dr. McDonald
Mr. Ryan
Governor Sanchez
Mr. Sandel
Senator Smith
Representative Whitaker

Against

Representative Arnold-Jones
Ms. Haynie
Senator McSorley
Mr. Morgan
Mr. Nathan
Senator Rawson
Representative Taylor

Highlights of Commission Meetings

April 24, 2003

Organizational meeting. Hiring of staff members Fred O'Cheskey, James P. O'Neill and Sharlene Shoemaker approved. Overviews of the tax system and issues of potential interest were presented by Secretary Jan Goodwin and Janet Peacock of the Legislative Council Service.

May 1-2, 2003

In-depth examination of the tax system and the sources and uses of revenues. Steering Committee created. Mr. Robert Cline, national director of State and Local Tax Policy Economics, Ernst and Young, discussed national and state-level trends, offered some suggestions on how the commission ought to approach its work — primarily that it should work from principles rather than dollars — and commented on the streamlined sales tax project. In accordance with its mission, the commission held a facilitated discussion about the strengths and weaknesses of the existing tax system and developed a consensus list of problems to be addressed. The main conclusions were that the evaluation of the tax system and alterations of it ought to be based on principles and that the following were the most visible problems: tax pyramiding in the gross receipts tax; application of the gross receipts tax to food and physician services; highway funding; and dissimilar treatment of businesses in like positions. (The full report is at Appendix B-8.) Secretary Jimenez reviewed the important revenue sources for state government and commented on what Governor Richardson hoped the commission would recommend. Mr. O'Cheskey outlined the history of New Mexico's tax policy.

May 22-23, 2003

Mr. Tom Clifford compared New Mexico's system with those of other states. He also presented data on the impact of the 2003 state phased-in cuts of personal income tax. Mr. Jim Eads, executive director of the New Mexico Tax Research Institute, explored the opportunities and issues with e-commerce. (As this report is being written, Congress is in the process of making permanent the ban on state taxation of Internet transactions and eliminating the grandfather clause that protected New Mexico.) After a discussion on the principles of taxation led by Commissioner McDonald, staff presented its consensus evaluation of how the New Mexico tax system stacks up based on those principles. (See Appendix B-9.) Mr. Bill Pound, executive director, National Council of State Legislatures, thoroughly reviewed the streamlined sales tax initiative. Mr. Robert Desiderio, chairman of the Professional Tax Study conducted in the 1990s, summarized the lessons to be learned from that tax reform effort. More detailed examinations of gross receipts tax pyramiding, the other state gross receipts taxes, local option taxes and compensating tax were presented.

June 12-13, 2003

The commission realized that its time was rapidly passing. It adopted the Steering Committee's proposal to split into four committees. The committees would meet during the commission's scheduled time until the August 11-12 meeting. The governor's extension until September 30 was announced. Each committee held its first meeting and presented its work plan to the full

commission. The commission also heard analysis of the impact of the 2003 federal tax bill on New Mexico. Secretary Jan Goodwin outlined ideas for streamlining and modernizing the tax administration system.

August 25-26, 2003

The full commission resumed hearings. The commission took testimony on the taxation of minerals, particularly coal, oil and natural gas. It was also given a briefing on the latest revision of the General Fund revenue estimates, which showed a small improvement. Each of the committees reported its recommended action options to the full commission. (These are presented at Appendices B-4 through B-7.)

September 11-12, 2003

The recommended options from the four committees were reorganized into nine "blocks" of options. (See Appendices A-1 through A-9.) A document was prepared and presented for each block explaining each option (and variations) and listing pros and cons for each. A summary table of fiscal impacts was included. The commission spent most of the meeting carefully hearing each option.

In addition, the commission heard at some length a pitch from Secretary of Economic Development Homans for development incentives the administration would like included in the commission's recommendations. Secretary Prukop of the Energy, Minerals and Natural Resources Department asked for consideration of measures to promote conservation.

Mr. Tom Clifford analyzed the 2003 income tax cut in depth. When fully implemented, personal income tax will raise \$350 million less than it would have prior to the cuts. Mr. Sam Flaim reported on the results of the first running of the state's new dynamic scoring model. The total package of significant revenue changes, according to the model, would actually reduce state jobs and tax revenues slightly. Although Mr. Flaim artfully avoided saying so, it was clear the model showed the 2003 state personal income tax reductions as an economic negative.

October 14, 2003

The final meeting, originally scheduled for September 29 and 30, was postponed after a meeting with the governor to await determination of whether a constitutional amendment authorizing use of permanent fund money for education had passed.

Action options agreed upon by the commission or suggested by individual commission members were added to the options developed by the committees. A separate document explaining those options and setting out pros and cons was prepared. (See Appendix A-10.) In all, 196 items were placed before the commission.

In order to facilitate an orderly discussion, the Steering Committee prepared a "straw man" table of selected options as the basis for action. The general revenue portion adopted a revenue neutral position while the portion dealing with highway issues was definitely revenue positive.

Drafts of each of the Steering Committee's options plus some of the others were distributed to the commission members. Commissioner Morgan offered an alternative table of options. Seventy-one items were adopted.

Commission Staff

The commission's staff consisted of three people: Fred O'Cheskey, James P. O'Neill (chief of staff) and Sharlene Shoemaker. Most of the commission's workload, however, was performed loyally and responsively by staff loaned to the commission by several organizations, particularly the Legislative Council Service and the Taxation and Revenue Department. The commission would like to specially recognize the contributions of the following people:

Legislative Council Service, Paula Tackett, Director

Amy Chavez
Cleo Griffith
Janice McCrary
Janet Peacock

Taxation and Revenue Department, Jan Goodwin, Secretary

Richard Anklam
Tom Clifford
Al Maury
Andy Seirp
Charles Stehwein

Legislative Finance Committee, David Abbey, Director

Steve Neel
Bill Taylor

Department of Finance and Administration, James Jimenez, Secretary

Sam Flaim
Melissa Vigil

Department of Transportation, Rhonda Faught, Secretary

Bo Alcott

Appendices

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- A-1 Streamlined Sales Tax Project and Proposal for New Mexico Participation
- A-2 Options for Tax Relief for Families
- A-3 Options for Reducing Taxation on Medical Services and Nursing Homes
- A-4 Options to Address Revenue Adequacy for Funding of Highway Maintenance and Construction and to Improve Equity
- A-5 Property Tax Options
- A-6 Options for Business Tax Reform and Relief
- A-7 Options for Reducing Horizontal Inequities in the Gross Receipts and Compensating Tax and Other Gross Receipts Taxes
- A-8 County Local Option Gross Receipts Tax Simplification Proposal
- A-9 Options for Reducing Horizontal Inequities, Balancing Rates and Making Other Changes in Selected Excise and Other Taxes
- A-10 Additional Options for Tax Reform and Relief

Volume 2

- B-1 Master List of Options (10/13/03)
- B-2 "Straw Man" Options Proposed by the Steering Committee
- B-3 Tax Reform Alternative (Commissioner Morgan)
- B-4 Report of the Economic Development Committee
- B-5 Report of the Equity Committee
- B-6 Report of the Family Committee
- B-7 Report of the Selective Excise Tax Committee
- B-8 Facilitated Discussion
- B-9 New Mexico Tax System and Top Ten Taxes Scorecard: A Self-Assessment by Internal State Tax Professionals

Volume 3

- C-1 Laws 2003, Chapter 77 (House Bill 168)
- C-2 Agendas, Minutes and Listing of Documents Submitted, by Meeting
- C-3 Public Hearing Notes
- C-4 Summary of Public Comments

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- D Text of Options in Bill Draft Form