

# ***Reforming the Gross Receipts Tax***

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# ***Martinez Administration Budget Priorities***

- **Sustainable budgets**
- Education reform
- **Competitive tax policies**
- Meeting fundamental needs
- Protecting public safety
- Efficient and accountable government

# ***Practical Tax Reform***

- Reform requires a balancing of competing goals of tax policy
  - Adequacy: 4 percent growth = Inflation + Population growth
  - Efficiency: Competitiveness = Key to economic growth
  - Equity: Horizontal (fairness) and Vertical (income distribution)
  - Simplicity: Taxpayer and state resources
- Goal is not the ideal tax system or the average tax system but improving on the current system in practical ways that don't disrupt the economy – taxpayers need predictability.
- Changes should be administrable without a dramatic increase in resources.

# ***Goals of Tax Reform***

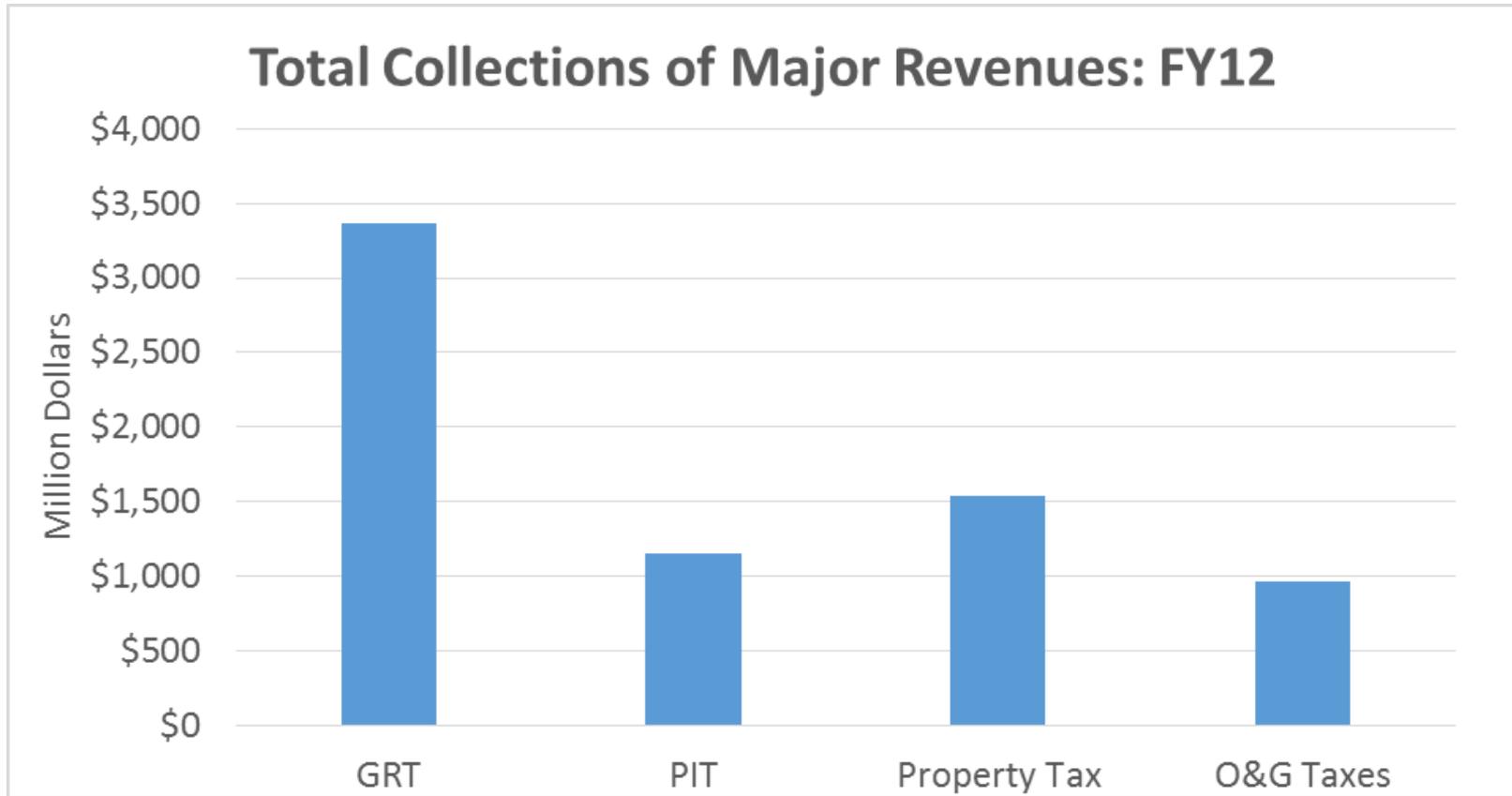
1. Help diversify the State's economy
2. Distribute benefits widely, limit use of targeted incentives
3. Continue to provide adequate revenue; if possible make revenue base more stable
4. Simplify administration and compliance

## ***Specific Issues With GRT***

- Large tax burden relative to other states
- Large burden on business-to-business transactions
- Regressive incidence if passed on to consumers
- Discriminates against in-state businesses competing with remote vendors
- Significant compliance burden that grows over time
- Traditionally reliable revenue source for State and Local Governments

## ***Starting Point for Reform***

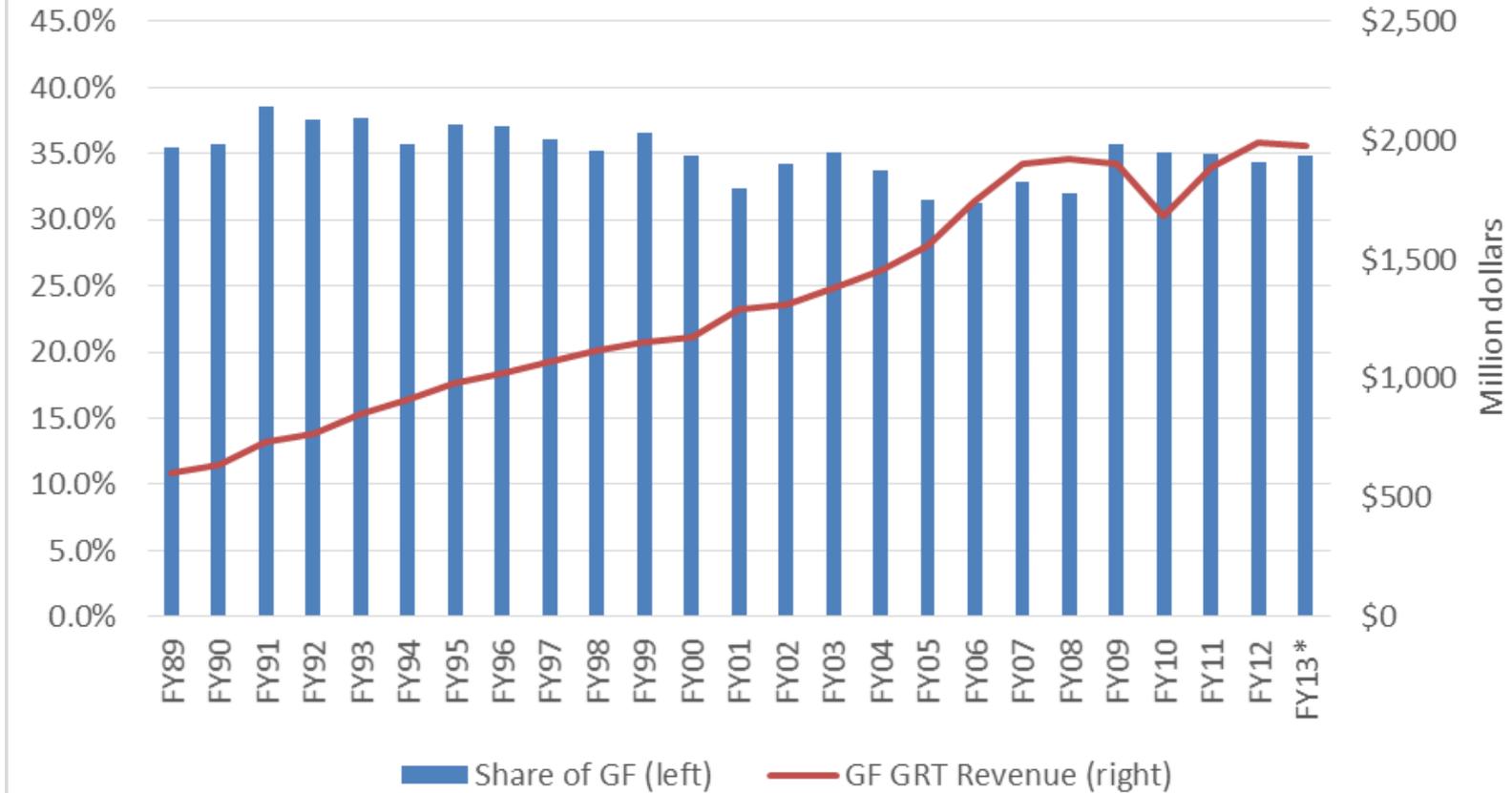
- NM has low property taxes, average income taxes and high sales taxes – the latter especially on business inputs.
- Revenue growth has been adequate to keep pace with population and inflation and also to allow for tax relief (PIT rate reductions, GRT deductions for food, health care)
- Revenue growth is unstable, heavily dependent on minerals production.



*GRT more than twice Property Taxes, almost 3 times PIT*

*GRT 1/3 of State General Fund; 75% of Muni taxes; 43% of County Taxes*

## General Fund GRT Revenue



*Compound growth rate:*

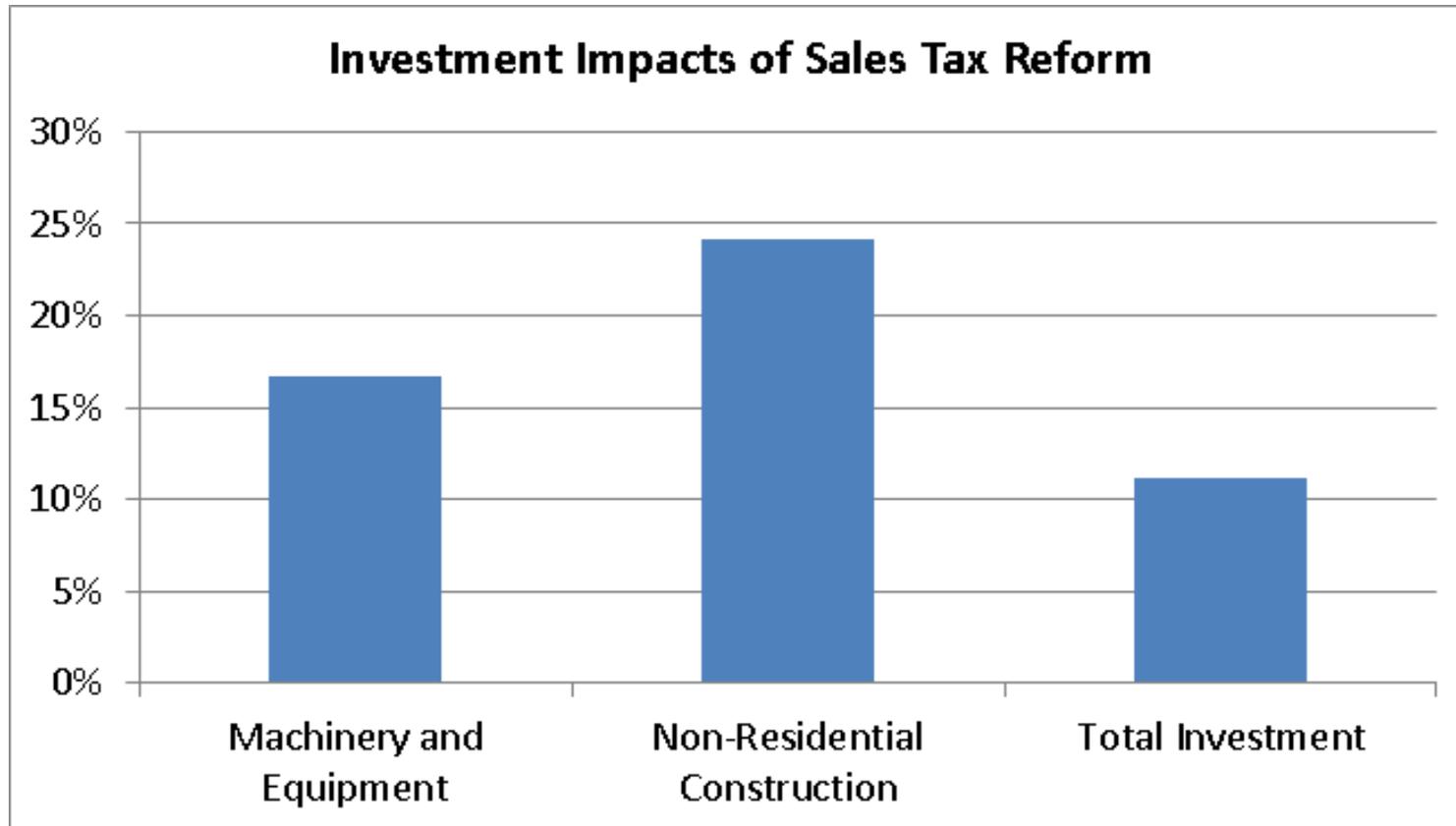
-- 1989 – 2007: 6.6%

-- 2007 – 2013: 0.6%

# ***Recent Changes In GRT Have Reduced Regressivity, Improved Competitiveness***

- Food & Medical Deduction: 2003
- Manufacturer pyramiding relief:2012
- Construction services/equipment pyramiding relief: 2012
- Tax incentive reform to improve targeting
  - High-wage jobs credit

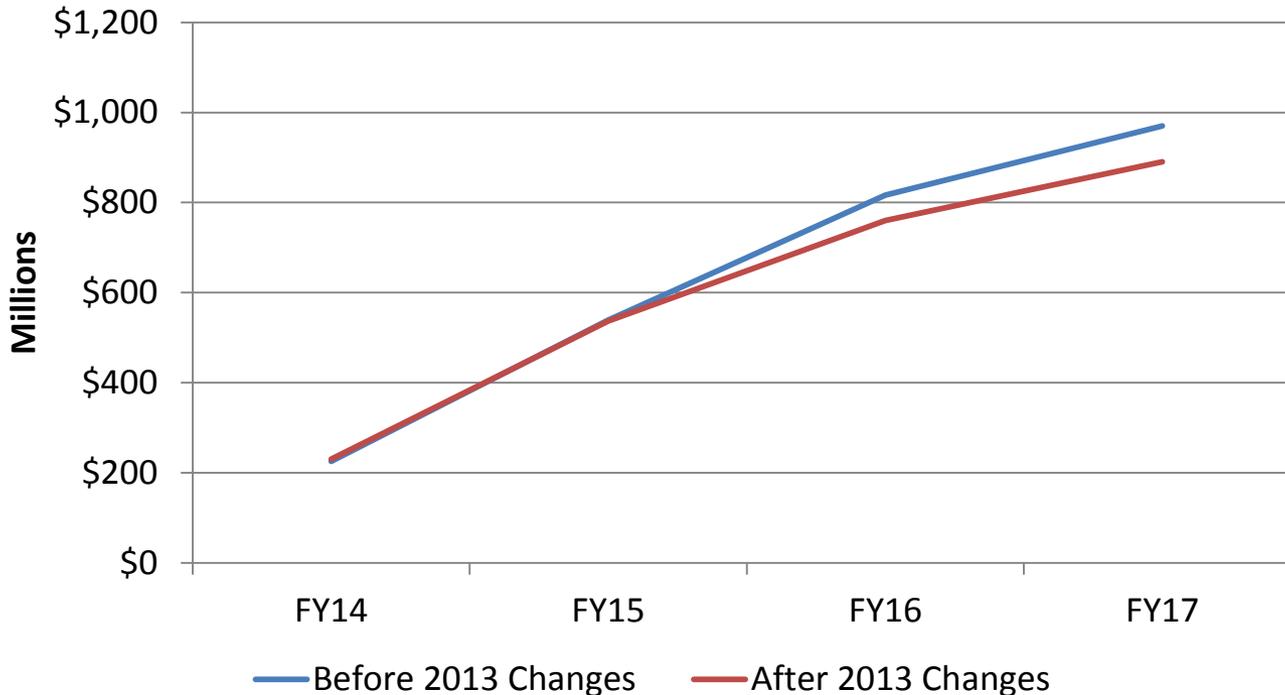
# Why Business Sales Tax Reform Matters



Source: Michael Smart and Richard Bird, *"The Impact on Investment of Replacing a Retail Sales Tax with a Value-Added Tax: Evidence from Canadian Experience,"* National Tax Journal, December 2009.

# Affordable Tax Reform

## Cumulative General Fund Recurring Revenue Growth



- Game-changing tax reform is affordable even under “static” scoring
- Less than 10% of forecast revenue growth is earmarked to tax reform
- Increased growth of less than 0.5% would fully offset all impacts

## ***Potential Incremental Reform: Small Business Tax Simplification***

- GRT deduction if total receipts less than \$50,000
- Annual GRT report would be matched with federal tax reports to prevent tax avoidance
- Half of all businesses pay 1% of tax
- GRT complexity is a significant burden for small business
- Small businesses are important to job creation

# ***Incremental Reform: R&D Pyramiding Relief***

- R&D services sold for re-sale
- NM is facing more competition for R&D procurement
  - Defense budgets under pressure
  - Industry consolidation
  - Foreign competition
- High-wage industry in which NM already has strong presence
- Current law R&D incentives not working

# ***Administrative Reforms***

- Independent hearing officers
- Apply uniform and more transparent rulemaking, audit and protest procedures
- Reform non-taxable transaction certificate rules to improve predictability

# ***Taxing Remote Commerce***

- 90% of remote commerce is business-to-business transactions
- Most of these transactions are deductible under state law: e.g. sales for resale
- Compliance on B2B transactions is relatively high, appears to be improving over time
- Increasing compliance would not be easily achieved
- Potential revenue gains from taxing remote commerce are limited

# *Conclusions*

- Incremental tax reform can make significant changes without disrupting the budget and while preserving predictability for taxpayers
- Recent changes have addressed regressivity, competitiveness issues within the GRT
- GRT continues to impose relatively high burden on business-to-business transactions
- Important areas to consider for reform include:
  - Small business simplification
  - Reducing the tax burden on R&D
  - Reforming administrative procedures to improve transparency