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## FISCAL IMPACT REPORT

ORIGINAL DATE 1-30-06

SPONSOR Smith LAST UPDATED \_\_\_\_\_ HB \_\_\_\_\_

SHORT TITLE Incorrect Gross Receipts Reporting Penalty SB 323

ANALYST Dearing

### REVENUE (dollars in thousands)

Estimated Revenue		Subsequent Years Impact	Recurring or Non-Recurring	Fund Affected
FY 2007	FY 2008			
(\$100.0)	(\$100.0)	Similar	Recurring	General Fund
(\$60.0)	(\$60.0)	Similar	Recurring	Local Governments

(Parenthesis ( ) Indicate Expenditure Decreases)

Duplicates HB 380

### SOURCES OF INFORMATION

LFC Files

#### Responses Received From

Taxation and Revenue Department (TRD)

### SUMMARY

#### Synopsis of Bill

Senate Bill 323 would amend Section 7-1-71.2 NMSA 1978 (being Laws 2004, Chapter 116, Section 3) effectively reducing the *doubling* of the difference between the correct and incorrect deduction claimed when in error as penalty, to only the amount, when there is an incorrect deduction claimed. Additionally, Section 7-9-47 NMSA 1978 (being Laws 1969, Chapter 144, Section 37), would amend the range of documents used to establish a nontaxable transaction for resale would be extended to include other documents to an approved list supplied by the Taxation and Revenue Department.

### FISCAL IMPLICATIONS

According to the Taxation and Revenue Department;

1. Under present law, deductions for food and medical services adopted in 2004, a penalty is imposed for taxpayer failure to correctly report the amount of the deduction. This penalty is imposed at the rate of *double* the local option tax rate in the business' location.

This legislative proposal would eliminate the doubled penalty rate, such that the penalty would be imposed at the rate of the local option taxes only, not a multiple thereof. In addition, a maximum upper-limit of \$10,000 would be set on the total penalty imposed.

2. Requirements for a seller to claim the gross receipts tax and governmental gross receipts tax deduction for the sale of property for resale would be modified. Under present law, the seller must receive a non-taxable transaction certificate from the buyer to be eligible for the deduction. The proposal would allow the seller to claim the deduction if provided other documentation to be specified by the Department.

Total collections of penalties under the double-local option have been approximately \$100,000 in the first year. An additional \$400,000 is currently protested. Experience suggests that a substantial portion of the latter amount will be abated. Thus, total collections are uncertain but probably about \$200,000 to \$300,000 per year. The proposal would reduce these by eliminating the double penalty and by imposing a cap of \$10,000.

These changes would be enacted effective July 1, 2006.

## **SIGNIFICANT ISSUES**

According to Taxation and Revenue department, if legislation is enacted, revenue would be impaired by approximately half of what is currently fined and collected under the current punitive measure. The amendment to 7-1-71.2 NMSA 1978 would negatively affect the general fund at a level of approximately \$100,000 annually, and would subsequently impact local governments at a negative level of approximately \$60,000 annually. It is unknown as to the level of impact that the \$10,000 penalty cap would have in decreasing current revenue from this source, however, this is not brought forward as a salient point by the Taxation and Revenue Department and is assumed to be minimal in comparison to the reduction of the multiplier.

## **ADMINISTRATIVE IMPLICATIONS**

According to the Taxation and Revenue Department, administrative implications of this legislation, if enacted, would include:

### *Double local option penalty:*

The double local option tax penalty has created a significant amount of confusion and conflict between taxpayers and the Department. Since many taxpayers view the penalty as unfair, they have been unwilling to voluntarily disclose misreporting that would be subject to the penalty. The Department has had to dedicate personnel to the task of assessing the penalty. Many of the taxpayers who have been assessed have protested the assessment. The protests have delayed collections and absorbed more Department resources to resolve. Reducing the penalty should encourage more voluntary compliance with the food and medical deductions, which will improve timeliness and accuracy of distributions at a reduced administrative and compliance cost.

### *Alternative evidence for deductions:*

For many years, gross receipts taxpayers have complained that they have been denied deductions they were legitimately entitled to because they did not receive an appropriate Non-Taxable

Transaction Certificate (“NTTC”) from the purchaser, sometimes through no fault of their own. The proposal would give the Department latitude to accept alternative forms of evidence proving eligibility for the deduction provided under Section 7-1-47 when an NTTC is not available. This will reduce administrative and compliance costs of the Gross Receipts Tax.

**CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP**

House bill 384 also amends Section 7-1-71.2, setting up a potential conflict if both bills are passed. HB 384 amends Section 7-1-71.2; however, the HB384 amendment does not affect the doubled-penalty element that is mentioned within the fiscal implications section of this report. *Instead, HB384 would amend (among other substantial changes) the doubled-penalty such that it is not applicable to those taxpayers who have entered into an agreement and are subsequently conducting a managed-audit with the Taxation and Revenue Department, however, it remains in place for those taxpayers who have not entered into a managed-audit agreement.*

**WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL**

If not enacted, Section 7-1-71.2 NMSA 1978, and Section 7-9-47 NMSA 1978 would exist as currently written.

PD/mt