F I S C A L I M P A C T R E P O R T

ORIGINAL DATE 02/21/11
SPONSOR Martinez, W.K. **LAST UPDATED** 03/11/11 **HB** 487/aHTRC

SHORT TITLE Create Direct Wine Shipment Permits **SB**

ANALYST Burrows

REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Non-Rec	Fund Affected
FY11	FY12	FY13		
	$20.0	$20.0	Recurring	General Fund – Annual Permits
	**	**	Recurring	General Fund – Liquor Excise
	**	**	Recurring	DWI Fund – Liquor Excise
	**	**	Recurring	General Fund – GRT
	(**)	(**)	Recurring	Local Govts Fund – GRT

(Parenthesis ( ) Indicate Revenue Decreases)

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY11	FY12	FY13	3 Year Total Cost	Recurring or Non-Rec	Fund Affected
		$57.0	$57.0	$114.0	Recurring	RLD Operating Budget
		$17.3	$0.0	$17.3	Nonrecurring	TRD Operating Budget

(Parenthesis ( ) Indicate Expenditure Decreases)

Duplicates SB445

SOURCES OF INFORMATION
LFC Files

Responses Received From
Attorney General's Office (AGO)
Economic Development Department (EDD)
Regulation & Licensing (RLD)
Taxation & Revenue (TRD)

Other Responses Received
The Wine Institute

SUMMARY

<u>Synopsis of HTRC Amendment</u>

House Bill 487 was amended to address several of the technical issues noted in the original synopsis. In particular, under the amended bill, permittees would be required to pay the liquor excise tax monthly, and would not be required to report annually on the amount of wine sold and shipped. The amendment also adds reference to subsection F in subsections A and B of Section 2 as was recommended in the original synopsis.

The amended bill would require the Regulation and Licensing Department to report the name and contact information of each permittee to the Taxation and Revenue Department upon approval of a permit application.

TECHNICAL ISSUES

As amended, the language would require payment of liquor excise tax in the month following the month in which liquor was sold and shipped *and* in which the permittee was issued a permit. Since permits are issued annually, this provision creates further confusion. A possible amendment would strike "issued a direct wine shipment permit" on page 3, line 11.

<u>Synopsis of Original Bill</u>

House Bill 487 adds a new section to the Liquor Control Act by creating a direct wine shipment permit that allows the holder of a New Mexico winegrower's license or the holder of a winery license in a state other than New Mexico to obtain a permit that will allow up to two cases of wine per month to be shipped directly to a New Mexico resident who is at least 21 years of age.

House Bill 487 establishes an annual application fee of $50.00 per permit for out of state wineries and no fee for New Mexico winegrowers. The bill limits the amount per case to nine liters. Cases must be conspicuously labeled "Contains Alcohol Signature of Person 21 Years or Older Required for Delivery."

The proposal would require permittees to register with the Taxation and Revenue Department (TRD), to make payment of liquor excise and gross receipts taxes at established intervals, and to provide annual reporting of the amount of wine sold and shipped. The bill would allow TRD to audit permittees, and would give New Mexico jurisdiction to resolve legal disputes that may arise.

House Bill 487 also amends Section 60-7A-3 NMSA 1978 to exclude persons holding winery licenses from shipping privilege reciprocity, which allows shipment of up to two nine-liter cases of wine per month from individuals or licensees in states that afford New Mexico reciprocal privileges under current law. New language extends the shipping privileges allowed by this proposal to holders of direct wine shipment permits.

The effective date of the provisions of this bill is July 1, 2011.

FISCAL IMPLICATIONS

The Alcohol and Gaming Division (AGD) estimates that perhaps 400 permits will initially be requested at $50.00 each for estimated annual revenue of $20,000. This is a conservative estimate as AGD has no way to determine the number of permits from out-of-state shippers. According to TRD, annual application fees would probably amount to no more than a few tens of thousands of dollars.

** TRD notes liquor excise tax receipts would likely be positive, assuming some unauthorized shipments are probably occurring now. Otherwise, any increased liquor excise tax from out-of-state wine is expected to roughly offset in-state wine sales, because the overall demand for wine would not likely be impacted by this legislation.

**TRD also reports that GRT impact will likely be positive, assuming wineries that are currently engaged in unauthorized direct shipment are incorporated into the tax system and tracked. Otherwise, any increased GRT from out-of-state sales is expected to be offset by some declines for in-state wine.

**Moreover, there could be a shift of gross receipts tax (GRT) revenue from the local governments to the general fund as New Mexico sales are replaced with out-of-state sales. Gross receipts revenue from out-of-state sales is not distributed to local governments. TRD reports the fiscal impact on local governments would likely be small.

TRD also notes the state cannot impose GRT on a business without sufficient physical presence in the state, also known as nexus. Some loss of GRT revenue may occur if direct wine shipments from out-of-state replace a substantial volume of sales within the state, and the out-of-state business fails to comply with tax payments.

Michigan provides a similar direct-to-customer wine shipping program as that proposed by House Bill 487. Using data obtained from Michigan's program and adjusting for population differentials, the Wine Institute estimates a net $200 thousand positive revenue impact to New Mexico from this proposal.

SIGNIFICANT ISSUES

RLD notes that direct wine shipments are not currently regulated, but are occurring in New Mexico. The state is not receiving any tax revenues on these sales. Moreover, the state has no way of tracking businesses that are shipping wine illegally to the state, and it has no mechanism for dealing with dispute or taxation issues. House Bill 487 could help address these issues.

However, if out-of-state wineries are already engaged in direct shipment with few repercussions, there may be little incentive for businesses to legitimize shipments through the permit process without more effective enforcement.

Under current law, New Mexico winegrowers are disallowed from direct shipment of wine within New Mexico. This proposal could benefit local winegrowers by expanding market size, which could provide an additional positive impact to local and rural economies.

According to the Wine Institute, New Mexico is the only state that currently allows reciprocal shipping privileges, so the exclusion of wineries from reciprocity privileges would have no impact (see Attachment).

TRD notes 37 states allow some (often limited volume) direct shipment by out-of-state wineries, and generally require a permit similar to that proposed in this bill. Twelve states prohibit sales to residents by out-of-state wineries. Montana allows out-of-state sales to residents holding a “connoisseur’s license,” but in practice, common carriers are unable to verify license-holders, so deliveries are not made in Montana.

ADMINISTRATIVE IMPLICATIONS

AGD would need a part-time FTE to review and process the direct shippers permit applications and to respond to inquiries regarding the permit process. Operating costs include staff time, increased postage costs, printing costs and costs for license certificates. The operating budget impact includes the salary requirements for one part-time FTE.

TRD notes an annual liquor excise tax report would need to be developed since taxpayers are currently required to file monthly for this tax. TRD will also need to develop an annual report to allow permittees to report wine sold and shipped in the prior year at a cost of about $2,000. A low impact on IT systems will involve about 170 hours or $15,300. Desk audit reviews could be conducted with existing resources.

DUPLICATION

Senate Bill 445 duplicates House Bill 487.

TECHNICAL ISSUES

Section 2 of Senate Bill 445 does not amend subsections A, B or C on pages 4 and 5 to reference the new subsection F. A possible amendment would include reference to subsection F in these subsections.

TRD reports the liquor excise tax is a monthly-filed tax program under current law. The department recommends the bill be amended to require *monthly* reporting of liquor excise tax. Since the taxpayer already has a monthly GRT reporting requirement, the addition of monthly reporting for the liquor excise tax does not seem excessively burdensome.

TRD would be unable to ensure tax compliance of out-of-state wineries. Only RLD has the authority to revoke the permit. A possible amendment to Section 1, subsection D on page 3 would require RLD to verify tax compliance, and provide for revocation of the permit if a taxpayer fails to make payments or file annual reports.

The AGO notes the bill does not address how this volume limit will be monitored or enforced. The state may face enforcement issues without specific provisions addressing how monitoring and enforcement of the proposed limitation will be carried out.

OTHER SUBSTANTIVE ISSUES

RLD questions whether the common carrier, UPS, FedEx and USPS, who would be responsible for verifying the age of the recipient, would be required to take an Alcohol Server Education class and have a valid permit to deliver alcohol. Additionally, it is unclear whether the state has the authority to mandate such a requirement from carriers.

RLD notes there is no fee required by this proposal for New Mexico winegrowers to obtain permits. This disparate treatment of New Mexico licensees and out of state licensees could result in litigation against the state for discriminatory practices.

TRD notes despite the bill's inclusion of a gross receipts tax filing requirement, accurate compliance might not be realized, and out of state audit undertakings might not be cost effective.

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL

New Mexico winegrowers and out-of-state wineries would not be able to direct ship wine to New Mexico customers.

LKB/bym:mew:svb

The Legislative Finance Committee has adopted the following principles to guide responsible and effective tax policy decisions:

1. ***Adequacy:*** *revenue should be adequate to fund government services.*
2. ***Efficiency:*** *tax base should be as broad as possible to minimize rates and the structure should minimize economic distortion and avoid excessive reliance on any single tax.*
3. ***Equity****: taxes should be fairly applied across similarly situated taxpayers and across taxpayers with different income levels.*
4. ***Simplicity****: taxes should be as simple as possible to encourage compliance and minimize administrative and audit costs.*
5. ***Accountability/Transparency:*** *Deductions, credits and exemptions should be easy to monitor and evaluate and be subject to periodic review.*

More information about the LFC tax policy principles will soon be available on the LFC website at www.nmlegis.gov/lcs/lfc