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FISCAL IMPACT REPORT

ORIGINAL DATE 1/25/21
 SPONSOR Pirtle LAST UPDATED 2/13/21 HB _____
 SHORT TITLE Waiver of Penalties on Certain Taxes SB 25/ec
 ANALYST Graeser

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY21	FY22	FY23	FY24	FY25		
Could be significant in the tens of millions; loss in FY21 followed by payment in FY22					Non-Recurring	General Fund (postponement of payments)
Could be significant – up to (\$6,000.0) each fiscal year					Non-Recurring	General Fund waiver of penalty and interest
Could be significant in the tens of millions; loss in FY21 followed by payment in FY22					Non-Recurring	Local Governments (postponement of payments)
Could be significant – up to (\$3,500.0) each fiscal year					Non-Recurring	Local Governments (waiver of penalty and interest)

Parenthesis () indicate revenue decreases

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY21	FY22	FY23	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
Total	\$18.0			\$13.0	Nonrecurring	TRD Operating***

Parenthesis () indicate expenditure decreases

SOURCES OF INFORMATION

LFC Files

Responses Received From:

Taxation and Revenue Department (TRD)

SUMMARY

Synopsis of Bill

Senate Bill 25 proposes a temporary (not-compiled) waiver of penalties and interest (P & I) on certain CRS (Combined Revenue System) taxes, including gross receipts tax, local option gross receipts tax or compensating tax liabilities, for failure to pay any taxes that became due

beginning on the date the Covid-19 public health order first came into effect (March 13, 2020) and ending two months after the public order is rescinded or expires. To receive the penalty and interest relief in this bill, taxpayers would still need to file tax returns timely but would not have to pay the tax owed by the 25th day of the third month after the public health order expires or is rescinded.

This bill contains an emergency clause and would become effective immediately upon signature by the governor.

FISCAL IMPLICATIONS

TRD notes the following considerations relative to the estimated revenue impact:

In FY19, penalty and interest for gross receipts tax (GRT) averaged approximately \$2.4 million per month. It is unknown how long the public health order will be in effect or how the ongoing COVID-19 pandemic will affect taxes owed and resulting penalty and interest; however, given normal taxpayer activity, this is a reasonable expectation of foregone revenues.

The temporary waiver of penalty and interest may induce taxpayers that would otherwise have paid timely to defer paying gross receipts and compensating taxes until the temporary provision expires. Depending on how long the public health order remains in effect, the bill may shift State and local revenues from FY21 to FY22.

LFC staff analysis notes the proposed retroactive waiver of P & I might be unconstitutional because P & I was routinely assessed by TRD from the time of filing through the date of payment of the taxes and accrued P & I. Once P & I has been assessed, it joins the underlying taxes as a debt owed the state or local governments and discharge or waiver is prohibited pursuant to the Constitution of New Mexico, Article IV, Section 32. (See “Technical Issues” below.) The estimate in the Revenue table assumes the retroactive provisions are unconstitutional, the provisions could be applied prospectively after the signing date, and the public health order will not be rescinded or canceled until after July 1, 2021.

However, waiver of P & I prospectively is constitutionally valid because the provisions of the bill prohibit assessment of P & I. What may likely happen, although it will be in practice rather than suggested or required by the language of the bill, is that a number of taxpayers will file their CRS-1 tax return, acknowledging a tax liability, but then not paying that liability until the last possible moment by the 25th of the third month¹

Thus, there will be two fiscal effects: (1) a delay in payments from the effective date of the provisions of the bill (the bill does carry an emergency clause and if passed by a supermajority of both houses, would be effective when signed by the governor. This would be inconsequential if the public health order were rescinded by March 31, 2021 but would become increasingly important for each month past that end of March date. For illustration, the following assumes that the public health order will expire June 30, 2021 and that 20 percent of total state and local GRT liabilities would be shifted to the 25th of the third month following expiration or rescission of the public health order would be approximately April 1, 2021). The amount of this delay in

¹ Taxpayers with larger monthly liabilities are required to pay by ACH processed at least a day before the 25th.

payments can be approximated as three months of revenue delayed times 20 percent of the total liabilities (this would be about 3 months x \$240 million x 20 percent = \$144 million for the state and about 3 x \$160 million x 20 percent = \$96 million). Because of the lag between declaration and payment, in this scenario about 5 percent of established liabilities may not be collected. This illustration would be the maximum potential assuming all taxpayers took advantage of the waived P&I and paid their tax liabilities at the last moment possible. However, notably, when similar provisions were granted in June 2020 special session (Chapter 4, Laws 2020), the state saw very little shifting of tax payments (although, many taxpayers had already filed and paid their taxes before the provision took effect).

Based on an analogy to taxpayer behavior noted in 2000 relative to the most recent general tax amnesty, many taxpayers, will notice that the provisions of this bill provide an interest free tax loan from the State of New Mexico to those gross receipts taxpayers. LFC staff prepared a table of general fund and local option gross receipts taxes. The table is based on RP-500 reports for the whole of FY19, FY 20 and FY21 YTD. This table is ATTACHMENT A.

The second and smaller, although an absolute loss rather than a shift of revenues between fiscal years, is created by the prospective waiver of penalty and interest for failure to pay taxes. The waiver on the \$48 million/\$32 million shifted creates an average of four months of 6.5 percent combined P & I or about \$12.5 million for the state and \$7.3 million for local governments. These P & I losses are split between FY 21 and FY 22 roughly equally. If TRD's estimate is closer to correct, then absolute losses would be in the range of \$5 million for the state and \$3.5 million for counties and municipalities. This assumes that the waiver of P & I would persist for about three months.

This bill may be counter to the LFC tax policy principle of adequacy, efficiency, and equity. Due to the increasing cost of tax expenditures, revenues may be insufficient to cover growing recurring appropriations.

SIGNIFICANT ISSUES

TRD notes the following significant issues:

This legislation provides temporary relief to businesses. The relief would help mitigate the impact of the economic downturn caused by the COVID-19 pandemic. The postponement of taxes due may allow a business to temporarily redirect those funds towards rent, payroll, and other necessary costs to keep the business operational without incurring penalty or interest on taxes.

Taxpayers would still be required to eventually remit gross receipts and compensating taxes incurred during the temporary provision, keeping local governments and the general fund essentially whole, except for any costs associated with the delay in receipt of the revenue. Costs of delaying cash flow are expected to be minimal for the State given its strong reserves, but some local governments may be more sensitive to cash flow delays associated with this bill. The delayed receipt of revenue facilitated in this legislation may lead to budget problems for local governments, which could impair their ability to make payroll, pay for necessary services, or result in an inability to pay bond debt service, thereby incurring their own penalties and interest.

LFC staff notes that although only gyms, small retail and restaurants were initially closed completely pursuant to the March 23, 2020 Covid-19 public health order, the provisions of the bill would apply to all gross receipts (and compensating) taxpayers. There have been a few modifications to the initial public health order, and it is somewhat uncertain if the bill's specification of "two months after the public health order expires or is rescinded" applies to the specific initial public health order or to subsequent amendments.

Details of the timeline of the Covid-19 experience in New Mexico are contained in the following url: <https://www.krqe.com/health/coronavirus-resources/timeline-coronavirus-in-new-mexico/>

The "Technical Issues" section of this FIR explain that the intended retroactive waiver of penalty and interest may be unconstitutional, since assessed P & I joins with the underlying taxes as a debt to state and local governments and such forgiveness of debt is prohibited by the Constitution of New Mexico, Article IV, Section 32.

PERFORMANCE IMPLICATIONS

With the potential for significant shifts of revenue from FY 21 to FY 22, concern is that agencies and local governments would be expected to curtail spending, initiate furloughs or otherwise have to curtail operations until the public health order finally expired or was rescinded.

ADMINISTRATIVE IMPLICATIONS

TRD asserts some administrative issues:

Information Technology Division (ITD) of the Taxation and Revenue Department estimates that the implementation of this legislation will require approximately one month and an estimated \$18,000 of contractual services costs. Outreach may need to be made to taxpayers including the issuing of letters and publishing an informational bulletin.

This would be difficult for TRD to administer. Ordinarily, TRD must have 90 days to implement complex systems changes. If the bill were passed and signed by the end of March 2021, TRD would have little flexibility to implement the provisions of the bill in a timely fashion.

TECHNICAL ISSUES

TRD notes the following technical issue:

On July 1, 2021, New Mexico will begin imposing local option compensating tax, similar to local option gross receipts tax. As drafted, the penalty and interest relief provided in the bill would not apply to local option compensating taxes if the relief were still in effect after July 1, 2021.

LFC staff contend that the retroactive waiver of P & I may be unconstitutional. This bill effectively proposes a retroactive amnesty, waiving penalty and interest for taxes incurred on taxes that were due beginning on March 23, 2020 and continuing until the effective date of the bill, provided that the taxes owed are eventually declared and paid. Additionally, the bill proposes a prospective amnesty for the period for taxes due beginning on the effective date of the bill until two months after the public health order expires or is rescinded. We can thus create a matrix of possibilities:

Class of Taxpayer	P & I status	Waiver Status	Constitutional?
Amount of P & I	6.5% total per month up to 10 months, then dropping to .5% per month		
Retroactive period (March 2020 to approximately March 31, 2021)			
Taxes declared timely and paid timely	None incurred	None	Yes, no waiver
Taxes declared timely and paid later	P & I due as specified	TRD assessed P & I monthly from declaration until payment.	Waiver not valid once P & I assessed. (1)
Taxes not declared timely; paid when declared.	Penalty for failure to file; no additional penalty or interest for failing to pay.	Per bill, no waiver for failure to file.	Yes, no waiver
Taxes not declared timely; paid later.	Penalty for failure to file; additional P & I for failing to pay for the period between declaration and payment.	Per bill, no waiver for failure to file, but TRD assessed P & I monthly from declaration until payment.	No waiver for failure to file; Waiver for failure to pay not valid once P & I assessed, (1)
Retroactive period (approximately April 1, 2021 to two months after cancellation or expiration of public health order: assume June 30, 2021 cancellation date)			
Taxes declared timely and paid timely	None incurred	None	Yes, no waiver
Taxes declared timely and paid later	P & I due as specified	Per bill, P & I not assessed each month from declaration until payment	Yes (2)
Taxes not declared timely; paid when declared.	Penalty for failure to file; no additional penalty or interest for failing to pay.	Per bill, no waiver for failure to file.	Yes, no waiver
Taxes not declared timely; paid later.	Penalty for failure to file; additional P & I for failing to pay for the period between declaration and payment.	Per bill, no waiver for failure to file, but P & I not assessed each month from declaration until payment	No waiver for failure to file; Waiver of P & I for failure to pay probably constitutional (2)

Explanation of Contention. Per AG opinion, once taxes have been declared, those taxes and penalty and interest assessed because of non-payment, they become a debt of the state and Article IV, Section 32 prohibits waiving of these debts. The counterargument is that the provisions of the bill prohibit TRD from assessing P & I for non-payment. Because the bill does not waive P & I for failure to file, this leads to a somewhat counterintuitive provision that the strategy to adopt is to file taxes timely, then not pay until the last possible moment.

From the effective date of the bill forward, the legislature can adjust the penalty and interest provisions. However, once the P & I has been assessed it becomes a valid debt owed the state or local governments. Again, the bill does not waive penalty and interest for failure to file, only failure to pay. This leads to the strategic recommendation to file timely during the prospective period and to pay at the last possible moment by the 25th of the third month following the rescission or expiration of the public health order.

Penalty and interest on tax owed not waivable. — Once the tax, penalty and interest has been established as a debt of the state, there was no power in tax commissioner to waive either the penalty or interest. 1958 Op. Att'y Gen. No. 58-126.

The pertinent constitutional section follows:

Constitution of New Mexico, Article IV, Sec. 32. [Remission of debts due state or municipalities.] No obligation or liability of any person, association or corporation held or owned by or owing to the state, or any municipal corporation therein, shall ever be exchanged, transferred, remitted, released, postponed or in any way diminished by the

legislature, nor shall any such obligation or liability be extinguished except by the payment thereof into the proper treasury, or by proper proceeding in court. Provided that the obligations created by Special Session Laws 1955, Chapter 5, running to the state or any of its agencies, remaining unpaid on the effective date of this amendment are void. (As amended November 4, 1958.)

The bill is carefully drafted to stay arguably within the stricture of Section 32. Although, in practice, there will be significant postponement of payments, with the likelihood that there will be significant revenue crossing from FY 21 to FY22, the bill contains no language that would suggest this strategy. The retroactive waiver of P & I will be constitutionally prohibited once P & I for failure to pay is assessed. That will be done automatically for the period from March 23, 2010 through approximately April 1, 2021. After that April 2021 date, however, the waiver provision becomes valid. TRD notes that there was a forgiveness of P & I enacted in the Special Session of 2020. This waiver was effective in June 2020 and waived P & I for three months.

The notwithstanding language of the bill may be similarly unconstitutional. If the bill proposed to amend the Gross Receipts and Compensating Tax Law as to the underlying liabilities, that would be within the prerogative of the legislature. Similarly, Sections 7-1-67 and 7-1-69 NMSA 1978, imposing penalties and interest for non-payment of taxes may be changed prospectively by bill.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

Relates to House Bill 6 of the 2020 1st Special Session.

OTHER SUBSTANTIVE ISSUES

TRD notes, “Penalty and interest for gross receipts and compensating taxes due from April 25th to July 25th, 2020 were waived under House Bill 6 of the 2020 1st Legislative Special Session so long as the taxpayer timely filed a tax return. The proposed language in this bill overlaps with this period, and as a result some of the relief called for in this legislation is redundant.”

LG/sb/al

ATTACHMENT A

	General Fund (\$ thousands)				Local Governments (\$ thousands)			
	Taxes	Penalty	Interest	Months delinquent	Taxes	Penalty	Interest	Months delinquent
Jul-18	\$220,392	\$719	\$396	22.1	\$154,515	\$493	\$270	21.9
Aug-18	\$235,034	\$843	\$391	18.6	\$156,584	\$571	\$245	17.1
Sep-18	\$239,628	\$1,093	\$542	19.8	\$158,122	\$749	\$311	16.6
Oct-18	\$231,604	\$852	\$518	24.3	\$156,207	\$498	\$317	25.4
Nov-18	\$225,045	\$802	\$387	19.3	\$152,133	\$567	\$260	18.3
Dec-18	\$249,703	\$954	\$526	22.0	\$170,530	\$522	\$316	24.2
Jan-19	\$225,402	\$974	\$1,203	49.4	\$151,621	\$538	\$278	20.7
Feb-19	\$214,492	\$985	\$548	22.2	\$144,882	\$636	\$309	19.4
Mar-19	\$241,228	\$1,028	\$534	20.8	\$162,956	\$700	\$349	19.9
Apr-19	\$239,967	\$714	\$378	21.2	\$158,596	\$473	\$256	21.7
May-19	\$237,685	\$873	\$595	27.3	\$156,513	\$602	\$347	23.1
Jun-19	\$252,728	\$1,001	\$498	19.9	\$178,372	\$611	\$293	19.2
FY19 Total	\$2,812,906	\$10,837	\$6,516		\$1,901,032	\$6,961	\$3,551	
FY 19 Average	\$234,409	\$903	\$543	24.0	\$158,419	\$580	\$296	20.4
Jul-19	\$256,348	\$986	\$468	19.0	\$194,976	\$651	\$291	17.9
Aug-19	\$258,819	\$974	\$541	22.2	\$163,494	\$572	\$266	18.6
Sep-19	\$277,440	\$1,105	\$675	24.4	\$185,832	\$676	\$381	22.6
Oct-19	\$266,944	\$856	\$545	25.5	\$169,312	\$537	\$277	20.6
Nov-19	\$243,162	\$810	\$407	20.1	\$157,191	\$544	\$239	17.6
Dec-19	\$291,897	\$1,216	\$816	26.8	\$185,757	\$830	\$591	28.5
Jan-20	\$251,317	\$952	\$546	22.9	\$158,323	\$637	\$319	20.0
Feb-20	\$258,149	\$820	\$379	18.5	\$148,132	\$521	\$260	20.0
Mar-20	\$263,084	\$788	\$322	16.3	\$162,441	\$556	\$223	16.1
Apr-20	\$229,492	\$1,070	\$380	14.2	\$140,112	\$681	\$262	15.4
May-20	\$234,680	\$1,237	\$706	22.8	\$152,801	\$736	\$376	20.4
Jun-20	\$254,620	\$1,148	\$579	20.2	\$167,869	\$680	\$321	18.9
FY20 Total	\$3,085,954	\$11,961	\$6,365		\$1,986,240	\$7,622	\$3,806	
FY 20 Average	\$257,163	\$997	\$530	21.3	\$165,520	\$635	\$317	20.0
Jul-20	\$231,914	\$120	\$487	162.0	\$159,276	\$87	\$292	133.7
Aug-20	\$233,009	\$1,344	\$484	14.4	\$157,299	\$926	\$367	15.8
Sep-20	\$252,492	\$576	\$402	27.9	\$166,625	\$455	\$206	18.1
Oct-20	\$235,312	\$732	\$401	21.9	\$152,383	\$451	\$179	15.9
FY21 YTD Total	\$952,727	\$2,773	\$1,774		\$635,583	\$1,918	\$1,043	
FY 21 YTD Average	\$238,182	\$693	\$444	25.6	\$158,896	\$480	\$261	21.8