New Mexico Taxes: Taking Another Look

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I. DEFINITION AND FACTORS OF A TAX

Taxes are the tool that governments use to transfer financial resources from the private sector to the public sector.¹ Taxes allow governments to raise the revenues necessary to finance publicly provided goods and services.² The amount and kind of taxes levied by a government depend on its fiscal needs and prevailing notions of tax principles and policies.

A tax is the product of two factors: (1) the tax rate and (2) the tax base. Thus, \( \text{TAX} = \text{TAX RATE} \times \text{TAX BASE} \). The characteristics of the tax rate and the tax base lie at the heart of discussions about tax principles and policies.

The tax rate is usually a percentage established by the legislature. Generally, the rate is fixed at a level that, when applied to the tax base, will produce the amount of taxes projected by fiscal planners. The tax base is the subject of the tax measured in dollars.³ The subject varies with the type of tax.⁴ For example, the tax base for a property tax is the value of the property, while the tax base for an individual income tax is a taxpayer’s “taxable income.” In most jurisdictions, general fund operations are financed by only a few tax bases: sales, income, value of property, and, in the western United States, the value of natural resources severed from the earth.⁵ By varying the tax rate and managing the tax base, legislators affect the amount of tax that taxpayers pay, while also achieving certain social and economic policy goals.

A tax cannot be imposed without designating the taxpayer. Moreover, it is important to know who ultimately bears the burden of the tax. The person statutorily obligated to pay the tax is the legal taxpayer.⁶ Thus, the individual who earns income is the legal taxpayer of the personal income tax. The legal taxpayer, however, may not be the person who bears the burden of the tax.⁷ For example, under the New Mexico gross receipts tax the legal taxpayer is the seller of the goods or services, but the person who bears the economic burden is normally the purchaser of the property or services.⁸ Likewise, the legal taxpayer of a corporate income tax

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³ See id. at 23.
⁴ Id.
⁶ See Hellerstein, supra note 2, at 21.
⁷ Id.
is the corporation that earned the income, but the persons bearing the burden of the tax are the corporation’s customers, suppliers, employees, and shareholders.\textsuperscript{9} A well-reasoned tax analysis will consider both the legal taxpayer as well as the party that actually bears the burden of the tax.

\section*{II. BASIC PRINCIPLES OF TAXATION}

Historically, governments have levied taxes to deal with changing economic needs, rather than to further some fundamental political theory.\textsuperscript{10} The New Mexico gross receipts tax, for example, is a product of the revenue crisis of the Great Depression.\textsuperscript{11} Recently, however, New Mexico has manipulated the tax system to influence economic development.\textsuperscript{12} Although lawmakers have used taxes to address different concerns during different times, the basic tenets of good tax policy have endured. As Adam Smith discussed in \textit{The Wealth of Nations}, these tenets include adequacy, equity, simplicity, and efficiency.\textsuperscript{13} It is nearly impossible, however, for any particular tax to satisfy all of these criteria at once.

\textit{Adequacy} is the ability of a tax system to generate sufficient revenue.\textsuperscript{14} Like any business, a government must have enough resources to fund its programs. When determining adequacy, it is appropriate to consider the ability of the system to endure within an evolving market. A system that fails to react to a new economic climate will eventually become obsolete because it lacks the flexibility to raise sufficient revenues in varying conditions.\textsuperscript{15} A tax system must not only produce enough income today, but it must also produce enough income in the future.\textsuperscript{16} Since the Depression, states have relied on sales or gross receipts taxes because these taxes are flexible enough to generate revenue even during slow economic times.\textsuperscript{17}

Recently, both income and sales taxes have proven to be productive revenue sources for state governments when levied on a broad base. In fiscal year 2002, gross receipts and selective sales taxes will account for $1.582 billion\textsuperscript{18} or forty-one percent of New Mexico’s total general revenues, while income taxes will produce just over $1.187 billion\textsuperscript{19} or thirty percent of total general revenues. Both of these taxes are designed to be flexible and adequate during slower economic times.

\begin{thebibliography}{99}
\bibitem{10} PECHMAN, supra note 1, at chs. 1, 5.
\bibitem{14} Id. at 2.
\bibitem{15} Id.
\bibitem{16} Id.
\bibitem{19} Id.
\end{thebibliography}
The second tenet of tax policy is equity. Equity is typically discussed in terms of two basic measures, horizontal equity and vertical equity.\textsuperscript{20} Horizontal equity generally relates to the tax base while vertical equity focuses on the tax rate.\textsuperscript{21} A system that achieves horizontal equity collects the same amount of taxes from taxpayers who have the same tax base.\textsuperscript{22} Vertical equity considers the manner in which tax rates rise or fall in response to changes in the income, or wealth, of taxpayers.

Horizontal inequity typically occurs when legislators pass laws allowing exclusions, deductions, exemptions, or credits to certain classes of taxpayers. Selective exclusions, deductions, or exemptions decrease the tax base of the taxpayers granted the benefit. If the tax is progressive, a reduction in the tax base may also impose a lower rate of tax upon a taxpayer, thereby moving the taxpayer from a higher to a lower tax bracket and compounding the resulting inequity. Although the tax base remains unchanged, the effect is the same when lawmakers allow credits. Credits directly reduce the amount of tax payable so that groups with otherwise similar incomes pay different amounts of tax.\textsuperscript{23}

Proportional, progressive, and regressive taxes embody each of the three approaches to vertical equity. A proportional tax is imposed at a flat rate so that all taxpayers remit the same percentage of their individual tax base. This type of tax can be viewed as the center of a continuum. At either end of the continuum lie the progressive and regressive taxes. Politicians and experts frequently debate which of these approaches best achieves vertical equity.

Under a progressive tax, taxpayers who earn more bear a greater portion of the tax burden.\textsuperscript{24} Thus, progressive taxes are commonly justified under the “ability to pay” principle.\textsuperscript{25} The best example of a progressive tax is the federal income tax. Taxpayers pay higher rates as their incomes rise. The opposite is true as incomes fall. The effect is to levy on a larger percentage of the income of higher-income individuals because they have a greater capacity to pay taxes. The progressive income tax also helps control inflation by moderating the amount of disposable income, or after-tax income, that taxpayers retain.\textsuperscript{26}

The final type of tax is a regressive tax. Under a regressive tax, taxpayers who earn less pay a higher percentage of their income in tax.\textsuperscript{27} The sales tax is the most recognizable example of a regressive tax. It constitutes the largest percentage of state tax revenues across the country.\textsuperscript{28} For example, consider two families, A and B, with after-tax incomes of $100 and $1000 respectively. Both families consist of four people, and each spends $100 in taxable purchases. Assuming a five percent sales tax rate, both families will pay five dollars in tax. Consequently, what looks to be a proportional tax because it is imposed at a flat rate is actually regressive.
Both families pay five dollars of tax but Family A pays five percent of its income in sales taxes while Family B pays one-half of one percent, one-tenth of A's rate.

**Simplicity**, the fourth principle of taxation, deals with a taxpayer's difficulty in complying with the tax law and the cost and effort required of the tax collector. The gross receipts tax, New Mexico's version of the sales tax, is considered a "simple" tax while the federal income tax is not. Simplicity is an important principle because a complicated tax may be theoretically sound but inadequate in practice because it is too difficult to administer, to comply with, or to enforce.

The final principle of taxation is **efficiency**. The less taxes affect the market decisions of consumers and producers, the more efficient the tax is considered to be. Conversely, taxes that substantially affect financial economic decisions are inefficient. Efficient taxes minimize loss of output from the private sector. Generally, the lower the tax rate, the more efficient the tax. Exemptions and deductions from the tax base are inefficient because they violate horizontal equity principles and result in tax-induced signals to consumers and producers.

Unfortunately, these criteria often conflict. For example, efforts to make a tax more equitable usually make it more complex. Furthermore, tax systems do not exist in an economic, social, or political vacuum, and tax laws are regularly used to promote other goals. Economic development is among the most prominent policy goals today, yet it often conflicts with the efficiency, simplicity, and possibly equity principles. As a result, some argue that economic development should be included as a fifth principle of tax policy. Tax-incentive economic development recognizes the use of the tax system to encourage businesses to locate in a jurisdiction or to commence growth projects. Economic development leads to increased employment, income, and consumption with a concomitant increase in tax revenue. At the same time, however, such tax incentives shift a portion of the tax burden away from new business and toward existing residents.

Certain points should be remembered when testing taxes against these policies:

1. The decision to follow one or more of the principles of tax policy represents a value judgment made by state policymakers.
2. Every legislative action changing taxes can be measured by one or more of the principles even if the legislature is unaware of the effect of the change. This is especially true when the action involves more than a change in the tax rate.
3. To get a true picture of its effects, state taxes must all be considered together (e.g., as a "tax system"). Many times a tax system will balance a negative policy decision on one tax with a more positive decision on

30. *Id.*
31. *Id.*
33. *Id.*
36. *Id.*
another. For example, New Mexico enacted the Low Income Comprehensive Tax Rebate in the Personal Income Tax Act to alleviate the regressiveness of the gross receipts and property taxes. Thus, when amending one tax, it is appropriate to consider its effect on the total tax system.

4. Further confusion arises from the fact that, as applied to a specific tax or the tax system, the principles of equity, simplicity, and efficiency often conflict. For example, the decision to provide a particular gross receipts tax exclusion may make the tax simpler because fewer people will be subject to the tax, but probably will result in horizontal inequity.

Lawmakers establishing a taxing structure must try to balance competing interests while maintaining the principles and policies that allow that structure to be grounded in reason. This is how New Mexico has structured its system. When considering reforms to this system, it is important to remember that the taxes that have been imposed must form an integrated unit.

Many economists and state tax experts believe that states should try to achieve balance in their state and local revenue systems. They often refer to state taxation as a “three-legged stool,” consisting of income taxes, property taxes, and sales taxes. They suggest that the legs of the stool should be of equal length in order to achieve a stable, productive, and predictable revenue stream. They also believe that diversifying revenue sources will protect states in times of economic depression. By decreasing their reliance on any one tax and maintaining a balance among potential revenue sources, state taxation systems build in stabilizers that can counteract shifts in the economy. Furthermore, balanced revenue sources affect other tax policy issues besides adequacy. A close look at New Mexico revenue sources helps illustrate this concept and highlights the reasons why this revenue balance is sometimes impossible to achieve.

III. NEW MEXICO TAXES

New Mexico’s tax system consists of many taxes: personal and corporate income taxes, gross receipts and compensating taxes, various other sales and excise taxes, a property tax, and severance taxes. The most important taxes in terms of generating revenue are the gross receipts and compensating tax, the personal income tax, the corporate income tax, the property tax, and the severance tax. Gross receipts and compensating taxes, income taxes, and severance taxes generate

38. Id.
39. In New Mexico, the stool has a fourth leg, the severance tax.
40. See Balance in State-Local Revenue Systems, supra note 5, at 1017.
41. Id.
42. Id.
43. N.M. STAT. ANN. §§ 7-2-1 to -35 (Michie 2001).
44. N.M. STAT. ANN. §§ 7-9-1 to -91 (Michie 2001).
45. N.M. STAT. ANN. §§ 7-12-1 to -17 (Michie 2001) (cigarette tax); N.M. STAT. ANN. §§ 7-13-1 to -18 (Michie 2001) (gasoline tax).
47. N.M. STAT. ANN. §§ 7-26-1 to -11 (Michie 2001).
seventy-eight percent of all New Mexico general revenues, while the property tax provides a large part of local government operating and capital needs and supports state and local bonds. Although New Mexico imposes other taxes, this article will only discuss these five taxes.

As is the case with most states, New Mexico taxes have always reflected the state’s current social and economic tenor. Our contemporary system began during the Depression. But New Mexico’s present tax system is not merely an aggregation of a series of isolated tax arts. Rather it is an integrated tax structure that was put in place between 1961 and 1975. The following brief history and scope of the five major taxes will illustrate this point.

A. Gross Receipts and Compensating Tax Act

1. Brief History

The Gross Receipts and Compensating Tax Act (GR&CTA) originated with the Emergency School Tax of 1935, which the state legislature enacted in the wake of the Great Depression. Like the GR&CTA, the Emergency School Tax was comprehensive and taxed nearly all retail sales of property and most services. The Emergency School Tax remained in place until 1966 when it was replaced by the current GR&CTA.

The GR&CTA has undergone two major structural changes since 1966. First, the state has permitted municipalities and counties to supplement GR&CTA with their own local “option gross receipts taxes.” These local option taxes have become the primary source of local operating revenues. Second, the base of the GR&CTA has been eroded by an increasing number of exclusions and deductions. Lawmakers enacted these exclusions and deductions for economic development purposes and they only benefit certain industries.

2. Basic Principles

The GR&CTA is a tax imposed for the privilege of engaging in business in New Mexico. Its purpose is to raise revenue by taxing most retail sales or leases of goods and services. The object of the tax is the gross receipts from the sale of goods and

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48. See Budget in Brief, supra note 18, at 4.
51. See id. (chronicling changes to New Mexico’s tax laws).
52. The Emergency School Tax was actually enacted in 1934 as a temporary sales tax. The 1934 act was reenacted in 1935 as a permanent gross receipts tax. NEW MEXICO TAXATION AND REVENUE DEPARTMENT, NEW MEXICO’S SALES TAXATION OF SERVICES: A PLAUSIBLE ONTOGENY, 13 (1996).
53. Id.
54. Id. at 5.
55. N.M. STAT. ANN. §§ 7-19D-1 to -12, 7-20E-1 to -21 (Michie 2001).
56. See Chavez, supra note 50, at 5.
58. See id.
Unlike a sales tax whose legal taxpayer is the buyer, the legal taxpayer for the gross receipts tax is the seller who customarily recovers the tax from the buyer through an increased sales price.

The state gross receipts tax rate is five percent. But local governments can impose an additional local option gross receipts tax (known as a rider) on the same gross receipts subject to the GR&CTA. The added imposition makes actual rates greater than five percent. The low rate is the 5.125 percent imposed in part of Catron County and the high rate is the 7.1875 percent imposed in Ruidoso.

The gross receipts tax is accompanied by the compensating tax, which is generally imposed on the value of goods bought out of state and brought into New Mexico. The compensating tax applies to transactions that would have been subject to the gross receipts tax if the transaction had taken place in New Mexico. The compensating tax is designed to prevent unfair competition that could arise if goods were purchased in another state with a lower tax rate and then used in New Mexico.

The compensating tax does not apply to services purchased out-of-state. For example, legal services provided in Texas would not be taxed in New Mexico. This creates horizontal inequity between the purchasers of goods and the purchasers of services. The compensating tax rate is five percent. Unlike the gross receipts tax, local and county governments cannot add a local option tax to the purchase of goods subject to the compensating tax. Therefore, the effective, statewide rate for the compensating tax is five percent.

In theory, the gross receipts tax is a consumption tax imposed on the amount realized by a seller from the sale or lease of goods and services. The tax attaches at the time of the sale or lease transaction. Sales occur both at the business and consumer levels, which makes the occurrence of pyramiding more likely. Pyramiding occurs where taxes are imposed upon a good or service more than once in the production process. To reduce pyramiding, the GR&CTA attempts to fix the taxing event at the point when the goods or services reach the consumer and exit the stream of commerce.

59. See id. Senate bill 148 proposes to provide a phased-in credit against the state portion of the gross receipts tax for receipts from the sale of food at retail food stores. This measure was not approved. S. Res. 148, 45th Leg., 2d Sess. (N.M. 2002). [hereinafter Proposed GR&CTA Food Credit].
60. In 1986, the legislature enacted a one-half of one percent taxpayer credit for transactions within municipal boundaries. The credit is actually paid to the municipalities in which the transactions occurred. This makes the actual state tax five percent for non-municipal areas and four and one-half percent within municipal boundaries. N.M. STAT. ANN. §§ 7-9-4, 82 (Michie 2001); See Chavez, supra note 50, at 7.
61. N.M. STAT. ANN. §§ 7-19D-1 to -12 (Michie 2001).
62. Telephone interview with Taxation and Revenue Department (Nov. 10, 2001).
63. N.M. STAT. ANN. § 7-9-7 (Michie 2001).
64. See id.
66. Id.
67. Id.
68. N.M. STAT. ANN. §§ 7-9-7 to 7-9-12 (Michie 2001) (imposing the compensating tax and denoting exemptions); N.M. STAT. ANN. §§ 7-19-1 to 7-39-10 (setting out New Mexico's tax system without allowing local or county compensating option taxes).
69. TAXATION AND REVENUE DEPARTMENT, SPECIAL REPORT 131 (July 1991).
3. Pyramiding

The Taxation and Revenue Department describes tax pyramiding as follows:

A tax is said to "pyramid" when it applies to more than one stage of production. Pyramiding is very uneven by nature, because its extent depends on the number of production stages, whether production is performed by one or many firms, how much is taxed at each stage, and whether the tax rate varies at each stage. Thus, some products may be heavily taxed due to pyramiding, and some will be taxed relatively lightly. Resulting differentials in effective tax rates cause distortions in economic decisions. For example, firms may integrate operations to avoid external transactions, or prefer to buy out of state rather than in state. Such distortions violate the neutrality criterion for judging the tax system.\(^7\)

Pyramiding falls into two principal categories: transactonal or direct pyramiding and indirect pyramiding.\(^7\) Direct pyramiding occurs when both the sale by a distributor to a retailer and the sale by a retailer to a consumer are taxed. Indirect pyramiding arises most often in the sale of services. For example, indirect pyramiding arises where a computer repair business hires a sub-contractor for a portion of the repair job and both the sale of the sub-contractor's services to the business and the sale of the business's services to the customer are taxed. The GR&CTA provides mechanisms to avoid most, but not all, direct pyramiding. But it provides few mechanisms to avoid indirect pyramiding.

Several conclusions about pyramiding can be drawn:

1. Virtually every industry suffers from some tax pyramiding under the GR&CTA. The GR&CTA taxes a broad range of goods and services, including goods and services sold to businesses. Since most businesses purchase goods or services from other businesses from time to time, and since it is customary to pass the gross receipts tax on to the customer as part of the price of the product or service, a transaction will effectively be taxed more than once.

2. Certain industries, such as the software and the electrical energy industries are subject to a greater level of tax pyramiding than other industries. Only a few sectors, however, suffer from material levels of transactional tax pyramiding under the GR&CTA because of the availability of deductions from the gross receipts tax base.\(^7\)

3. While very few industries suffer from significant levels of tax pyramiding, virtually all suffer from some form of indirect tax pyramiding. Depending on the industry, indirect tax pyramiding may or may not be significant. A 1988 study by the Taxation and Revenue Department determined that twenty-five percent of the GR&CTA yield can be attributed to indirect pyramiding.\(^\text{73}\)

\(^{70}\) Id.

\(^{71}\) Tax pyramiding also results when other taxes (generated under different tax systems) are added to the price of the product or service produced and passed on to the consumer. For example, a manufacturer's price for his product includes (as an overhead item) a portion of personal and real property taxes paid by the manufacturer. New Mexico's low property taxes mitigate the effects of this type of situation.

\(^{72}\) See N.M. STAT. ANN. §§ 7-9-45 to -91 (Michie 2001).

\(^{73}\) TAX RESEARCH AND STATISTICS OFFICE, NEW MEXICO TAXATION AND REVENUE DEPT., ESTIMATED
4. A taxpayer’s ability to take advantage of the GR&CTA’s provisions eliminating transnational tax pyramiding may depend on his or her sophistication and resources. Many of the GR&CTA’s provisions are complex and difficult to apply. As a consequence, a particular taxpayer may not realize that it is possible to avoid tax pyramiding by structuring a particular transaction or contract in a particular way. As a result, the GR&CTA system favors sophisticated taxpayers with access to more resources.

4. Exemptions and Deductions

Exemptions are legislative exclusions from the GR&CTA tax base. For example, the GR&CTA exempts wages, interest, and dividends from the tax base because these exemptions prevent pyramiding and are returns on labor or capital, as opposed to receipts from the sale of goods or services. Theoretically, the purpose of an exemption is to remove those transactions that are not consistent with the GR&CTA’s conceptual construct. GR&CTA exemptions generally cover transactions with governmental and tribal agencies, transactions subject to other taxes, receipts that do not comport with the definition of gross receipts or that may not be taxed, and transactions involving certain industries or entities such as charitable organizations. Not all exemptions create a clean conceptual construct, nonetheless exemptions are a useful and important tool for tax craftsmen.

Deductions, on the other hand, exclude receipts that meet the theoretical definition of gross receipts but may be subtracted from the tax base for policy reasons. A good example is a distributor’s sales of inventory to retailers. If a distributor is not permitted to deduct inventory sales to retailers, the value of the inventory will be taxed twice and result in pyramiding. GR&CTA deductions involve a variety of sections enacted for different purposes. Some deductions are intended to prevent pyramiding, while others are designed to provide an indirect subsidy to certain industries. Still others exist for administrative reasons. The practical difference between an exemption and a deduction is that a taxpayer need not report exempt gross receipts, but must report gross receipts when seeking a deduction.

5. Governmental Gross Receipts

The GR&CTA contains the governmental gross receipts tax (GGRT), which applies to New Mexico governments. The rules applicable to the GGRT generally mirror the statutory principles applicable to gross receipts and compensating taxes. The GGRT rate is five percent. It is imposed on any agency, instrumentality, or institution of the government, or any political subdivision (collectively known as


74. N.M. STAT. ANN. §§ 7-9-17, -25 (Michie 2001).
78. N.M. STAT. ANN. § 7-9-4.3 (Michie 2001).
79. Id.
"agencies"). School districts and certain health care providers licensed by the Department of Health are excepted. The taxable activities under the GGRT are the following:

1. Receipts from the sale of taxable personal property other than water from facilities open to the general public;
2. Receipts from recreational, athletic, or entertainment services or events in facilities open to the general public;
3. Receipts from refuse collection, disposal, or both;
4. Receipts from sewage services; and
5. Receipts from the sale of water by a publicly owned entity.

The policy behind the enactment of the GGRT is to put governmental agencies that venture into the open market on equal footing with private institutions. In this way, the gross receipts tax is imposed on goods and services provided by the government in the same manner as those provided by private citizens. The rationale for the GGRT is that agencies that engage in the listed activities would compete unfairly with private business if they were exempt from all gross receipts taxes.

Many agency activities, however, are not subject to tax. For example, the GGRT does not include receipts for health care services by a public hospital or tuition received by public education institutions. As a result, some agencies compete with private organizations engaged in similar activities without paying taxes on their gross receipts.

The GGRT has some important limitations. Since the state is constitutionally prohibited from directly taxing the federal government, federal agencies and activities are not subject to the GGRT. Since no GGRT is imposed or collected on the competitive activities and services performed by the federal government, the federal government enjoys an advantage over its private competitors.

B. Personal Income Tax (PIT)

New Mexico first imposed an income tax in 1919. Similar to the current PIT, that tax was progressive. Rates ranged from a low of one-half of one percent for taxable income between $5,000–$10,000 to a high of three percent for taxable income over $50,000. In 1961, New Mexico enacted a withholding tax and established its present system of “piggy-backing” onto the federal personal income tax. This means that New Mexico uses the same definition of adjusted gross income (AGI) as the IRS and taxpayers enter their federal AGI figure on both their federal and state income tax returns. Since 1961, there have been a number of changes to the PIT, most of which fall into four general categories: (1) changing the
tax rate, (2) changing New Mexico tax law to reflect amendments to the Internal Revenue Code, (3) enacting tax rebates such as the Low Income Comprehensive Tax Rebate (LICTR), and (4) requiring periodic estimated tax payments.  

1. Changes in Tax Rate

New Mexico applies a progressive tax rate that ranges from 1.7 percent to 8.2 percent.  

New Mexico's top tax rate of 8.2 percent is higher than the top rate in most states that impose a personal income tax. Taxpayers also reach the 8.2 percent rate at a lower income than in other jurisdictions. The top rate applies to single taxpayers with a taxable income of at least $65,000 and married taxpayers with a taxable income of at least $100,000. But, the top effective rate is actually lower than 8.2 percent. The effective rate is lower because state income taxes are deductible from federal gross income. Since New Mexico uses federal adjusted gross income (gross income less exemptions and deductions) as the base for its personal income tax, New Mexico personal income taxes are also deductible from state income. Consequently, the top effective rate for PIT is 7.5 percent, not 8.2 percent.

2. Changes That Reflect Amendments to the Internal Revenue Code

During the past 40 years, Congress has made many changes to the Internal Revenue Code that have affected the definition of adjusted gross income and taxable income. New Mexico automatically adopted most of those changes, but in some cases needed to amend the PIT to maintain the integrity of the piggyback system.

3. Enactment of the Low-Income Comprehensive Tax Rebate (LICTR) and Similar Rebates

LICTR, enacted in 1972, is probably the single most important change to the PIT since its inception. LICTR is more than a typical credit. Taxpayers who qualify for LICTR may receive a refund even if the amount of the credit exceeds the taxpayer's taxable income. Qualifying taxpayers are low-income families as defined in the PIT. The amount of the rebate ranges from $10 to $450, depending on the taxpayer's income and the number of personal exemptions. In effect, LICTR is a negative income tax.

The purpose of LICTR is to return a portion of the gross receipts, property, and other state and local excise taxes to low-income taxpayers. In a sense, LICTR makes the gross receipts and property taxes less regressive and makes New Mexico's

89. See Chavez, supra note 50 (chronicling the various changes to New Mexico's tax code over the last century).
90. N.M. STAT. ANN. § 7-2-7 (Michie 2001).
92. N.M. STAT. ANN. § 7-2-7 (Michie 2001).
94. See Chavez, supra note 50, at 33.
95. Id. at 32, 33.
96. Id. at 32.
97. N.M. STAT. ANN. § 7-2-14(A) (Michie 2001).
overall tax system more progressive, or, at least, proportional. Unfortunately, many low-income families in New Mexico do not receive LICTR's benefits because they do not file tax returns.

Since 1972, the state legislature has tinkered with LICTR because of revenue needs and changes in New Mexico's economic climate. Furthermore, the legislature implemented a separate medical rebate in 1975 and added a food rebate in 1979. These rebates made the gross receipts tax less regressive by returning some of the tax paid to low-income taxpayers. In 1977, lawmakers also passed a property tax rebate for senior citizens. Like LICTR, the property tax rebate serves to return to low-income individuals some of the property taxes they pay. This makes the property tax less regressive. The one difference is that most of the gross receipts taxes go to the state, while local governments retain property taxes. Still, the state rebates general fund revenues to make the property tax more equitable.

4. Estimated Taxes

Prior to 1997, taxpayers who failed to pay or remit sufficient withholding taxes from their paychecks were not required to make periodic tax payments to the state. Under the Internal Revenue Code, however, they had to make quarterly payments to the federal government. In 1997, the legislature brought New Mexico tax law into line with federal tax law. Since then, taxpayers who fail to remit sufficient withholding taxes must make quarterly tax payments to the state. This helps level the state's revenue stream and keeps taxpayers from owing unexpectedly large amounts of tax at the tax deadline.

C. Corporate Income Tax (CIT)

The New Mexico legislature enacted the first CIT in 1919 and passed the current law in 1961 when the legislature amended the CIT to conform with the federal corporate income tax. Technically, the 1919 CIT applied to both personal and corporate income, while excluding the income of banks, financial institutions, and insurance companies. In 1981, legislators finally separated the CIT from the PIT. Like the PIT, the CIT "piggybacks" onto the Internal Revenue Code's corporate income tax. Taxable income for the CIT is generally the same as the taxable income a corporation reports on its federal tax return. Piggybacking provides some federal–state uniformity and makes it simpler for taxpayers to complete their returns.

98. See Chavez, supra note 50, at 32, 35, 37.
99. After many legislative changes to the medical and food rebates, they were repealed altogether in 1993. See id. at 32, 33, 35.
100. See id. at 32.
101. See Budget in Brief, supra note 18, at 10.
102. See Chavez, supra note 50, at 36.
103. Id.
104. Id. at 27, 28.
105. Id. at 27.
106. Id. at 33.
All states have faced the difficult issue of implementing a constitutional method of taxing income attributable to the state. This is difficult because New Mexico and other states cannot constitutionally tax income earned by a corporation out of state. In 1961, New Mexico joined many other states in passing the Uniform Division of Income for Tax Purposes Act (UDITPA). UDITPA's apportionment and allocation methods attribute income earned by a corporation engaged in interstate commerce to New Mexico only if the income has an appropriate relationship to the state. To make administration and tax collection easier, New Mexico entered into the Multistate Tax Compact in 1967.

New Mexico offers local corporate affiliates of national enterprises the broadest reporting options of any state. A corporation may file as a single, local corporation and use UDITPA to attribute income to New Mexico. A corporation may also choose to combine the national income of all the corporations, both local and national, and then attribute the proper share of income to New Mexico under UDITPA. Corporations and their affiliates may also choose to base the group's New Mexico tax return on its federal consolidated tax return. In 1993, the legislature made a major change to UDITPA by allowing manufacturers like Intel the option of double-weighting their sales income. The double-weighted sales apportionment option reduces the corporate income tax for corporations that manufacture products in New Mexico but sell the majority of their products outside the state. These options give corporations the best of all worlds, because they allow corporations to choose the reporting option that produces the lowest tax obligation. Most states do not provide such a wide array of reporting options to their in-state corporations. The downside, however, is that once a corporation selects a method, it is difficult to switch to another.

D. Property Tax

New Mexico has levied a property tax since territorial times. Before the Great Depression, the property tax served as New Mexico's revenue mainstay and acted

110. N.M. STAT. ANN. §§ 7-5-1 to -7 (Michie 2001); See Chavez, supra note 50, at 28.
111. N.M. STAT. ANN. §§ 7-5-1 to -7 (Michie 2001).
112. There are three reporting options for corporate filers and New Mexico allows corporations to choose any one of the three.
116. N.M. STAT. ANN. § 7-4-10 (Michie 2001).
117. See id. STATE POLICY REPORTS describes the effect of increasing the weight of the sales factor: Increasing the weight of the sales factor in income apportionment formulas has been touted as an economic development tool because firms with physical plant and payrolls in the taxing state would bear smaller tax burdens than they would under a factor apportionment formula giving equal weight to all three factors. In addition, the increased weight given to the sales factor allows states to tax the income earned in the state from sales by out-of-state firms. The Rise and Fall of State Corporate Income Taxes, STATE POLICY REPORTS (Federal Funds Information for States, Washington, D.C.) Oct. 2000, at 2, 9 [hereinafter Rise and Fall].
119. See Chavez, supra note 50, at 1-89.
as the vehicle for funding public education.\textsuperscript{120} The Depression exposed one of the principal drawbacks of a property tax. When real property values fell dramatically, statewide property taxes also plummeted.\textsuperscript{121} The ensuing revenue crisis led to the enactment of the severance tax and, a short time later, the Emergency School Tax, which helped ease the revenue shortfall.\textsuperscript{122}

With the return to prosperity, two additional property tax problems surfaced. First, it became apparent that property taxes depend upon assessments of property value. In New Mexico, local authorities value real property and those valuations are not uniform throughout the state. Second, wealthier counties enjoy higher assessed values and thus greater tax revenues. The consequence of both phenomena was that funding for public schools was disproportionate.

In the late 1970s, courts across the nation began hearing more lawsuits challenging the constitutionality of public school funding systems similar to New Mexico’s system.\textsuperscript{123} Against this backdrop, New Mexico changed its method of financing its public schools.\textsuperscript{124} The legislature developed a public school equalization formula that appropriated school money on the basis of the number of students and local property values.\textsuperscript{125} In theory, poorer school districts received the same amount of money \textit{per student} as wealthier districts with the same number of students. As a result, property taxes stopped funding public school operations in the early 1990s.\textsuperscript{126}

Today property taxes play a very small role in the funding of state programs and New Mexico ranks forty-ninth nationally with respect to the amount of property taxes its citizens pay.\textsuperscript{127} The state government only uses property taxes to support general obligation bonds (G.O. bonds), but local governments continue to rely heavily on property taxes.\textsuperscript{128} Property taxes support city, county, and local school district bonds, and they also pay for some local operational activities.\textsuperscript{129}

New Mexicans maintain a historical and deeply felt aversion to property taxes. This aversion originated in territorial days when many landowners lost their property in tax-foreclosure sales.\textsuperscript{130} The problem came to a head in the Great Depression when bankruptcies and tax foreclosures on agricultural land created severe hardship for landowners.\textsuperscript{131} Citizens responded strongly enough to prompt the

\begin{itemize}
\item 120. \textit{Id.} at 8–11.
\item 121. See generally, \textbf{DAVID. T. BEITO, TAXPAYERS IN REVOLT: TAX RESISTANCE DURING THE GREAT DEPRESSION} (1989).
\item 122. See \textit{Chavez}, supra note 50, at 1.
\item 123. Memorandum from Robert J. Desiderio, Dean, University of New Mexico School of Law, and James La Fata, Student, University of New Mexico School of Law, to New Mexico Public School Capital Outlay Task Force (July 2000) [hereinafter Public School Capital Outlay Memo] (on file with author).
\item 124. \textit{Id.}
\item 125. \textbf{N.M. STAT. ANN.} § 22-8-25 (Michie 1978).
\item 126. \textit{See Public School Capital Outlay Memo, supra note 123.}
\item 127. \textit{HOVEY, supra note 91, at 148.}
\item 129. \textbf{N.M. STAT. ANN.} § 6-15-4 (Michie 2001).
\item 130. See generally \textit{BEITO, supra note 121.}
\item 131. \textit{Id.}
\end{itemize}
legislature to amend the state Constitution to limit most local property tax levies to twenty mills.\textsuperscript{132}

This aversion to property taxes also stems from the fact that the taxes may be unrelated to a taxpayer's ability to pay. This is especially true in places like Santa Fe and Taos, where out-of-state residents have moved in and bid-up the price of high-end homes. These higher prices inflate the value of all homes in those areas and the counties' periodic property tax valuations quickly capture the increase. Although county officials may lower mill rates, few counties choose to do so when property values increase.\textsuperscript{133} Similarly, support for county bonds nearly always mandates maintaining mill rates.\textsuperscript{134} Thus, property tax obligations increase as valuations increase, which puts additional strain on low- and middle-income property owners, whose tax bills frequently increase faster than their incomes.

\textbf{E. Severance Tax}

The state legislature originally enacted the New Mexico Severance Tax in 1933, one year before the Emergency School Tax, and it too is a product of the Depression.\textsuperscript{135} The New Mexico Supreme Court stated the policy reasons for imposing a severance tax when it upheld the constitutionality of the Severance Tax Act in \textit{Flynn, Welch & Yates, Inc. v. State Tax Commission}.\textsuperscript{136}

The state in effect says to the producers: Your operations deplete the natural resources of the state, and to the extent that you remove from the earth the natural wealth with which nature has provided it, and to the extent you impoverish it, you are required to pay a license tax for the use and benefit of the state, for the privilege of extracting such natural wealth. The tax is not on the...[resource], but rather upon the business of producing...[the resource] based upon annual production.\textsuperscript{137}

The removal of the resource from the earth is the subject of the severance tax. The tax is usually imposed on the value of the resource when it is severed from the land.

Since 1934, legislators have made three types of changes to New Mexico's resource taxes. First, they enacted a separate Oil and Gas Severance Tax in 1959.\textsuperscript{138} Second, lawmakers added a number of resource-related taxes to the New Mexico tax statutes.\textsuperscript{139} Third, the legislature has changed the resources covered by the various taxes and the tax rates applied to each resource many times over the years.\textsuperscript{140}

Interestingly enough, the most important revisions to the severance taxes have not been to the taxing statutes themselves but to the use to which the taxes are put. In

\begin{flushright}
132. N.M. CONST. art. VIII, § 2.
134. N.M. CONST. art. IX, § 13.
135. See Chavez, supra note 50, at 43.
136. 38 N.M. 131, 137, 28 P.2d 889, 892 (1934) (quoting State v. State Board of Equalization, 17 P.2d 68, 72 (Mont. 1932)).
137. Id.
138. See Chavez, supra note 50, at 45.
139. These additions include the Oil and Gas School Tax, the Natural Gas Producers Tax, the Oil and Gas Conservation Tax, the Oil and Gas Ad Valorem Tax, the Oil and Gas Production Equipment Ad Valorem Tax, and the Resources Excise Tax. See Chavez, supra note 50, at 47-49.
140. Id. at 43–50.
\end{flushright}
1973, New Mexico created the Severance Tax Permanent Fund as the repository for severance taxes not reserved for payment of severance tax bonds. Under the present legislative scheme, fifty percent of severance taxes secure "senior" severance tax bonds (long-term bonds) and 37.5 percent back supplement bonds, as well as other short-term bonds issued to fund public school and higher education capital projects. The remaining 12.5 percent of the severance taxes are deposited in the Severance Tax Permanent fund. The present value of the Severance Tax Permanent Fund is approximately $4 billion; 4.7 percent of the fund is distributed to the New Mexico general fund annually and appropriated by the legislature.

IV. SOURCES AND APPLICATION OF NEW MEXICO'S REVENUES

Current economic conditions always directly impact the amount of tax revenue that a state can generate. As the economy slows, spending and incomes fall, and tax bases shrink and generate less revenue. Economic growth is often an issue both in New Mexico and elsewhere.

New Mexico personal income growth has been revised downward from almost 6 percent to about 5 percent for the current year. New Mexico currently ranks 40th in the country in wage and salary growth over last year and continues to lag behind other states in this region in terms of economic growth.

In 2002, state spending became a national issue when the economic downturn caused sharp revenue declines at both the state and federal levels. Declines such as these force legislators to make tough spending decisions.

A. Sources of Revenue

New Mexico obtains tax revenue from several sources. In fiscal year 2000, the state collected $1.582 billion in general and selective sales tax revenue, which constituted approximately forty-one percent of expected total state general fund revenue. Income taxes represented the second leading source of general fund revenue. They generated $1.187 billion or thirty percent of the general fund revenue. New Mexico's natural resources taxes, rents, and royalties contributed another $586 million, or fifteen percent of general fund revenue. The state's investment of its permanent funds and reserves produced $466 million, or twelve

141. See Chavez, supra note 50, at 44; N.M. STAT. ANN. § 7-27-3 (Michie 2001).
144. N.M. CONST. art. VII, § 10.
145. "U.S. economic growth has slowed significantly in the last few months. Third quarter GDP growth in 2000 was 2.4%, the slowest rate in four years. This compares with 5.7% growth the previous year. Growth is expected to be moderate—3 to 3.5% per year—in the forecast period." See infra Table 1, Budget in Brief, supra note 18, at 3.
147. Id. at 4 (showing Table 2: General Fund Consensus Revenue Estimates).
148. Id.
149. Id.
percent of general fund revenue. Finally, $82 million, or two percent of general fund revenue, came from miscellaneous sources.

B. Application of Funds

State general fund expenditures continue to finance primary and secondary education. Almost fifty percent of the state's general fund expenditures go to public schools. Higher education (fifteen percent), health and human services (twenty-one percent), general government (ten percent), and public safety (seven percent) make up the remainder of the expenditures. It is important to note that the above data reflects only general fund revenues and expenditures. General fund revenues represent approximately fifty percent of the state's total budget. The other fifty percent comes from specifically targeted revenues; the most significant of which is the Road Fund. Gasoline excise taxes are allocated to this fund.

C. Local Impact

As a percentage of combined state and local taxes, local government taxes account for a relatively small percentage of the total taxes collected in New Mexico. A survey in 1996 by State Policy Reports indicates that New Mexico ranks third overall in the percentage (seventy-nine percent) of the total tax burden levied at the state, rather than the local level. The primary reason for this is that the state funds public school operations in New Mexico, while local governments fund schools in other states. Nevertheless, any change in New Mexico's gross receipts tax and property tax structure will still dramatically affect local revenues.

As discussed previously, New Mexico has historically relied upon the property tax as its principal local revenue source. Although the property tax remains important today, gross receipts taxes now have a greater impact on local government. In New Mexico, the legislature permits both municipalities and counties to levy a separate gross receipts tax in addition to the one imposed by the state. The state government administers and collects the tax as an additional percentage of the same gross receipts tax base used by the state. Municipalities may add an additional .5 to 2.3125 percent, while counties may impose an additional...
to .75 percent. The county percentage can be greater in designated counties for designated projects such as corrections facilities, county-supported Medicaid, or local hospitals. In addition, municipalities receive 1.225 percent of all gross receipts taxes collected by the state from taxpayers in the municipality. Consequently, local governments have a stake in maintaining a comprehensive gross receipts tax base.

When New Mexico enacts or expands exclusions or deductions, both the state and local government receive fewer gross receipts taxes. The resulting revenue loss impacts local governments more than the state government because gross receipts revenues constitute a larger percentage of local budgets than the state budget. The local impact is also amplified because local governments have fewer alternative revenue sources.

Property taxes present a somewhat different issue for local governments. The Property Tax Act applies uniformly throughout the state, but local governments may impose their own mill levies for statutorily approved purposes. In general, the property tax system is locally administered, and the appropriate county collects the tax. This means any legislative change to the Property Tax Code or the tax bonding statutes related to property taxes will affect local governments.

D. State and Tribal Taxation

New Mexico's tax system is also influenced by dual sovereignty. The term "dual sovereignty" refers to the right and authority of both the state and Indian tribes and pueblos to govern the land and people within their boundaries. Any discussion of state taxation in New Mexico must consider the authority of Indian nations to tax on Indian lands. While New Mexico's state government possesses the authority to impose taxes upon its citizens and its lands, the tribes and pueblos also possess the authority to impose taxes on their citizens and their lands. Dual sovereignty can result in dual taxation of the same event by both the state and the tribe or the pueblo. Thus, the taxpayer may be unduly burdened when both governments attempt to tax the same transaction.

Most observers conclude that dual taxation hinders economic development on Indian lands. State and Indian governments tax in order to generate enough

162. N.M. STAT. ANN. §§ 7-19-12, 7-19D-9, -12 (Michie 2001).
163. Id. §§ 7-20C, E, F.
164. Id. §§ 7-19, -20.
166. N.M. STAT. ANN. § 1-23-3 (Michie 2001).
168. BLACK'S LAW DICTIONARY 1401 (7th ed. 1999).
169. St. Louis v. Wiggins Ferry Co., 78 U.S. 423, 429 (1870) (explaining that power of taxation for purposes of commonwealth is part of all governmental sovereignty and is inseparable from it) (citing Merrion v. Jicarilla Apache Tribe, 455 U.S. 130, 141 (1982) (holding, "The power to tax is an essential attribute of Indian sovereignty because it is a necessary instrument of self-government and territorial management. The power . . . derives from the tribe's general authority, as sovereign, to control economic activity within its jurisdiction, and to defray the cost of providing governmental services by requiring contributions from persons or enterprises engaged in economic activities within that jurisdiction").
170. Richard J. Ansson, Jr., State Taxation of Non-Indians Whom Do Business with Indian Tribes: Why Several Recent Ninth Circuit Holdings Reemphasize the Need for Indian Tribes to Enter into Taxation Compacts
revenue to satisfy their wants and needs. When different sovereigns compete for finite resources, the struggle results in heavy tax burdens, revenue shortages, and lost business.

The state has no clear authority to tax events on Indian land. After considering the state’s interest in the activity being taxed, the burden of the tax on tribal interests, and federal policies, it remains unclear whether federal treaties and statutes preempt this kind of state action.\textsuperscript{171} It is evident that states cannot tax tribes or Indians engaging in on-reservation activities;\textsuperscript{172} however, state governments possess broad authority to tax non-Indians on Indian land.\textsuperscript{173} The exercise of this authority can result in the heavy burdens of dual taxation, especially in mineral development.\textsuperscript{174}

Both the state’s authority to tax non-Indians and the extent of Indian taxing authority remain unclear.\textsuperscript{175} How those jurisdictional lines are drawn will certainly affect the ability of sovereigns to generate revenue. Indian tribes and pueblos hold nearly nineteen percent of the non-government land in New Mexico.\textsuperscript{176} State and local governments lose a potential source of revenue if they lack the power to tax on those lands.\textsuperscript{177} Tribes bear a potential loss, however, when the state succeeds in taxing on Indian lands.

Losses can take different forms. For example, when businesses leave tribal lands, the tribes lose revenue, jobs, and access to the services and products supplied by those businesses. Tribal governments also suffer when they must forego taxation to keep businesses from leaving. To avoid intergovernmental conflict and the burden of dual taxation, the authority of each jurisdiction to tax must be determined. Recent efforts have focused upon cooperation between state and tribal governments in joint administration, audit, and tax collection.\textsuperscript{178} The goal is to develop an acceptable method to avoid double taxation on tribal lands.

The thorny issues of dual sovereignty also arise in the area of Indian gaming. Although not technically dual taxation, the issue of competing for limited tax dollars surfaces here as well. Before Indian gaming came to New Mexico, taxpayers’ entertainment dollars generally were funneled into the state’s economy where they theoretically increased the gross receipts and income tax bases. Today, casinos secure a portion of the entertainment dollars formerly relied on by the state.

On the one hand, this redirection of taxpayers’ disposable income negatively impacts the state’s ability to generate revenue by decreasing the gross receipts tax

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\textit{with Their Respective State, 78 OR. L. REV. 501, 543 (1999).}
\textsuperscript{172} Id. (citing Montana v. Blackfeet Tribe of Indians, 471 U.S. 759, 764 (1984)).
\textsuperscript{173} Slade, supra note 171, at 15.
\textsuperscript{174} Id.
\textsuperscript{175} Ramah Navajo School Bd., Inc. v. Bureau of Revenue of New Mexico, 458 U.S. 832, 838 (1982) (stating a “rigid rule” of state taxing powers in Indian country does not exist); Slade, supra note 171, at 16 (stating, “preemption of state taxing power must be analyzed on the facts of each specific case”).
\textsuperscript{176} NEW MEXICO TAXATION AND REVENUE DEPARTMENT, SPARRING GROUND FOR INDIAN-STATE TAX ISSUES 1 (1996).
\textsuperscript{177} Id.
\textsuperscript{178} H.R. 549 (N.M. 1996).
\end{flushleft}
On the other hand, the increase in employment created by the casinos might compensate for the loss in gross receipts tax by increasing the income tax base. Furthermore, the state might benefit not only from casino-employee income taxes but from the re-injection of the disposable net income of those employees into the state’s economy. The pueblos and the governor have negotiated and approved new revenue-sharing agreements, and the legislature, in its oversight role, has approved those agreements.180

V. EROSION OF THE TAX BASE

Because a tax is the product of its two basic elements, the tax rate and the tax base, as long as the tax rate does not change, a reduction in the tax base will cause tax revenues to decline. This base reduction is often referred to as erosion. In recent years, the explosion of remote sales has brought this issue to the forefront of state efforts to streamline their tax systems.181 Furthermore, the decline in corporate income tax revenue182 and the relative stagnation of the New Mexico economy in comparison to surrounding states have also affected the state’s revenue prospects.183 Erosion of the tax base could be the primary problem in New Mexico state taxation today.

A. Remote Sales

Since catalog sales emerged some years ago, a shift has occurred from face-to-face transactions to a less personal and non-local means of doing business. The rate at which this change is occurring is increasing exponentially because of technology, particularly the Internet.184 This shift has raised a debate over who has jurisdiction to tax these sales. The primary inquiry is which state should have the right to impose a tax on the sale of goods.185

Sales (gross receipts) and use (compensating) taxes have always been imposed based on the destination principle, meaning that the state where the buyer uses or consumes the product has the authority to impose the tax.186 Where an in-state buyer purchases from an in-state seller, the gross receipts tax is imposed at the point of purchase.187 But when the buyer is out-of-state, the seller is not obligated to collect

179. The Taxation and Revenue Department estimates that $1.13 billion is displaced from the gross receipts taxable economy to the non-taxable economy.
182. Corporate income tax revenues have declined as a percentage of state revenue, not in dollars collected. See Rise and Fall, supra note 117, at 18-88.
184. There is evidence that the e-commerce explosion might not be having as dramatic an impact on tax revenues as the literature leads us to believe. It is estimated that sixty-five percent of e-commerce involves business-to-business sales that would not be subject to gross receipts taxation were they “face-to-face” transactions. See infra Tables 4 and 5, E-commerce and State Sales Tax Losses, State Policy Reports (Federal Funds Information for States, Washington, D.C.), Sept. 2000, at 10, 11.
185. See E-Commerce and the States, supra note 181, at 17.
186. Id. at 14.
187. Id.
the tax. Instead, the buyer is responsible for remitting a use tax to the state where the product will be put in service. The problem with this system is the practical difficulty of enforcing it. Either consumers are not aware of their obligation to remit the use tax, or they know that they stand little chance of being caught. Thus, New Mexico does not require consumers to pay the compensating tax on catalog or Internet purchases.

The abstract nature of electronic commerce exacerbates this problem. Not only is it impossible to characterize a web-retailer as physically present in any one state, but also the kind of goods and services that such a retailer provides are often electronic, such as on-line music. Because it is so difficult to determine the point or destination of an Internet purchase, it is extraordinarily hard to know how to apply the tax.

In addition to the practical difficulties inherent in imposing a tax on Internet sales, many constituents who engage in e-commerce have pressured federal lawmakers to keep these transactions tax-free. In response, Congress has imposed a moratorium on the authority of states to tax e-commerce transactions and effectively eroded the retail sales base from which states may generate revenue.

Not all states have opposed the ban. The governors of Virginia, Colorado, and Massachusetts have advocated for a permanent moratorium on state taxation of Internet commerce. These governors have stated that public policy concerns dictate that Internet commerce remain a tax-free zone and that they believe a moratorium is the best way for states to support that goal. Granted, the negative impact of e-commerce erosion would probably be less in these states than elsewhere. Sales taxes constitute the smallest percentage of revenues from the major revenue-producing taxes (property, sales, and income) for both Virginia and Massachusetts, and Colorado’s diverse revenue sources would minimize the impact of lower sales tax receipts.

In contrast, states opposing the moratorium argue that exempting e-commerce companies gives them a competitive advantage over other retailers. Together with private-sector representatives, leaders of these states have tried to streamline tax administration to create a viable sales tax collection system for complex e-commerce sales. This effort coincides with House and Senate committee discussions of

188. Id. at 15.
189. Id.
190. N.M. STAT. ANN. § 7-9-7.1 (Michie 2001) (limiting the state Department of Taxation and Revenue’s authority to collect the compensating tax).
192. See E-Commerce and the States, supra note 181, at 17.
194. See E-Commerce and the States, supra note 181, at 17.
195. See Taxing the Internet, supra note 193, at 18.
196. Id.
197. Id.
199. See Taxing the Internet, supra note 193, at 18.
200. Id.
whether Congress should extend the Internet tax moratorium.\textsuperscript{201} The interstate debate matches those states that rely less on sales taxes or that have large e-commerce constituencies against those states that are more dependent on sales taxes and less beholden to e-commerce.\textsuperscript{202} New Mexico has not joined the states participating in the streamlined sales tax project.\textsuperscript{203}

B. Corporate Income Tax

A recent trend in state corporate income taxes also deserves attention. "Although state corporate profits tax collections have grown steadily for the past four decades, their relative importance in state revenue systems has declined since the 1980s."\textsuperscript{204} Chart 3 shows that state corporate profits tax collections have represented a progressively smaller percentage of total state tax collections since 1980. The most significant drops occurred during recessions, specifically 1981-83 and 1989-91.\textsuperscript{205} But since 1995, the relative importance of corporate income taxes has declined even as corporate profits have risen.\textsuperscript{206} This paradox is difficult to explain.

Three factors have contributed to the decline in the importance of corporate income taxes: measurement errors, growth of more aggressive and sophisticated tax planning, and actions by state policy makers.\textsuperscript{207} Measurement errors refer to the effect of the growing use of pass-through entities such as subchapter S corporations (corporate entities taxed as a partnership), limited liability partnerships, and limited liability corporations.\textsuperscript{208} When businesses organize themselves under one of these forms, their profits are classified as corporate, but they do not pay taxes at the corporate level.\textsuperscript{209} Instead, all profits flow through and are taxed at the shareholder level.\textsuperscript{210} As a result, the taxes are considered individual income tax revenue rather than corporate income tax revenue.

The growth of state tax planning has also affected the extent to which states may rely on the corporate income tax.\textsuperscript{211} Specifically, the ability of businesses to establish out-of-state holding companies allows them to shift income from high-tax states to low-tax states. This income-shifting has also impacted the amount of corporate income tax states can collect.\textsuperscript{212}

State economic policy decisions have also played a role in the declining importance of corporate tax revenues.\textsuperscript{213} In New Mexico, the impact of these decisions on revenue is apparent from the enactment of economic development incentives.\textsuperscript{214} "In addition to broad-based tax rate cuts, which benefit all firms, state

\textsuperscript{201} See E-Commerce and the States, supra note 181, at 17-18.
\textsuperscript{202} Id.
\textsuperscript{203} Id.
\textsuperscript{204} See Rise and Fall, supra note 117, at 18. See infra Charts 2 and 3.
\textsuperscript{205} Id.
\textsuperscript{206} Id. at 3.
\textsuperscript{207} Id. at 18-22.
\textsuperscript{208} Id. at 6.
\textsuperscript{209} Id.
\textsuperscript{210} Id.
\textsuperscript{211} Id. at 8.
\textsuperscript{212} Id.
\textsuperscript{213} Id. at 9.
\textsuperscript{214} See infra section VII.
NEW MEXICO TAXES

officials have added numerous incentives to their corporate income tax codes to retain existing firms and to attract new ones. Today, nearly every state offers incentives for job creation, research and development, investment in designated locations, while many have incentives for providing child-care. Furthermore, New Mexico, like a number of other states, has changed its income apportionment formulas to decrease the tax burden on corporations.

It is difficult to accurately measure how these three factors have decreased the relative importance of the corporate income tax. It is clear, however, that the factors emerged as a result of interstate competition to attract business capital. States view the corporate income tax as an economic development management tool. They offer corporate income tax incentives in hopes of bolstering their economies by attracting big corporate business. The usefulness of this method of interstate competition, however, remains questionable.

C. Economic Growth

A final source of erosion relates to weaknesses in New Mexico’s economy. Comparisons to national labor market and income statistics compiled by the State Budget Division of the Department of Finance and Administration show that New Mexico lags behind other states. Between 1999 and 2001, U.S. personal income growth has increased 5.6 percent. In New Mexico, the increase was only 3.6 percent. The disparity between wage and salary growth likewise favors the national economy, which increased by seven percent while New Mexico’s rate increased by 4.3 percent. If New Mexico’s economy cannot keep pace with the rest of the country, the state’s overall tax base will continue to lose ground and its ability to produce future revenue may fall short of the state’s needs.

215. Id.
216. Id.
217. Id.
218. Id. at 10.
219. Id.
220. Id. Economists do not necessarily advocate the race to the bottom:
Most economists suggest that state policy makers should maintain a stable business tax climate with low rates and broad tax bases that can efficiently support the level and types of public services desired by both individuals and businesses, rather than ad hoc “competitive” tax reductions. Some also have noted that over-reliance on tax reductions as the preferred means for competing for mobile business often leads state and local governments to provide less than optimum levels of services, and that sub optimum levels of public services can actually retard economic development. See Rise and Fall, supra note 117, at 10.

221. See Table 1, Gov. Gary E. Johnson, State of New Mexico Budget in Brief and Capital Budget, Fiscal Year 2002, Dec. 31, 2000, at 3.
222. Id.
223. Id.
224. Id.
VI. COMPARISON OF NEW MEXICO' S TAXES TO THOSE IN OTHER JURISDICTIONS

A. New Mexico and Surrounding States Generally

A comparison of New Mexico's tax system to systems in six surrounding states (Arizona, California, Colorado, Oklahoma, Texas, and Utah) demonstrates that New Mexico's tax system is competitive at both the personal and business levels. The comparison included gross receipts and sales, other excise, severance, income, and property taxes paid directly by households and businesses. This does not mean that there is no room for improvement.

New Mexico imposes average taxes on low and middle-income households. California and Colorado have generally levied lower taxes on these brackets than New Mexico, while Arizona, Oklahoma, Texas, and Utah have imposed higher burdens on low and middle-income taxpayers. Conversely, New Mexico's taxes on high-income households were near the highest in this region.

While New Mexico's low and middle-income tax burden is average, its property taxes are strikingly low. New Mexico imposes the second lowest property taxes in the nation, both on a per capita basis and as a percentage of state personal income tax. This undoubtedly results from the extremely low tolerance of New Mexicans for property taxes.

Surprisingly, the average low and middle-income tax burden and the low property tax burden do not result in a lower than average tax burden. As a percentage of per capita income, the burden (state and local taxes combined) on the citizens of New Mexico is actually higher than the burden on the citizens of surrounding states.

The high tax burden as a percentage of per capita income figure is due to New Mexico's low per capita income. New Mexico's per capita income in 2001 was $21,835. This figure explains why single taxpayers with $65,000 of taxable income and married taxpayers with $100,000 of taxable income are in the state's top tax bracket. New Mexico also collects the highest amount of taxes in the region. California is second, with Oklahoma and Utah tied at third.

Among the surrounding states, New Mexico's taxes on corporations that do not generate income from the severance of natural resources were the lowest. Despite

226. Id.
227. See BBER, supra note 225, at 86.
228. Id. at 87.
229. Id. at 87; See also HOVEY supra note 91, at 154, 157 (containing tables of Individual Income Taxes and the Highest Personal Income Tax Rate by state).
230. Id.; see also HOVEY supra note 91, at 147, 148 (setting out Property Taxes and Property Taxes per Capita by state).
231. HOVEY, supra note 91, at 142.
232. See id.
233. Id. at 155.
234. Id. at 143.
235. See BBER, supra note 225, at 64-66 (including tables that compare the combined tax burden on manufacturing firms and for-profit service firms as well as other types of businesses in cities of comparable size in Arizona, California, Colorado, New Mexico, Oklahoma, Texas, and Utah).
these low taxes on extractive industries, New Mexico still imposes a heavier overall burden than nearby states.\(^{236}\)

**B. Gross Receipts Tax**

The design of New Mexico’s GR&CTA attempts to minimize the regressive impact on low-income taxpayers. The GR&CTA tax base includes food, most non-hospital care, and services.\(^{237}\) Both Oklahoma and Utah also tax food consumed at home.\(^{238}\) New Mexico taxes neither food purchased with federal food stamps nor prescription drugs.\(^{239}\) Both of these exclusions reduce the regressive aspects of the GR&CTA.

Additionally, the gross receipts tax on services also makes the tax less regressive as well as less popular because high-income households spend more of their income on personal services. The GR&CTA’s broad base allows New Mexico to have the lowest gross receipts rate of the seven surrounding states.\(^{240}\) This means that, overall, New Mexicans do not pay the highest amount in gross receipts taxes.

**C. Gross Receipts Taxes on Businesses**

It is difficult to accurately assess the effects of the gross receipts tax on business activity. Businesses vehemently object to the gross receipts tax on services.\(^{241}\) Assessing the actual gross receipts tax burden requires considerably more research but there are inherent barriers to this research because of the number of variables that impact the gross receipts tax.\(^{242}\)

In general, the gross receipts tax might apply at two different points in the production process. The first is at the sale of goods or services by the business; presumably this tax is passed on to the customer. The second point where a business may pay gross receipts is on the purchase of services as business inputs.\(^{243}\)

Any comprehensive measurement of the tax burden at the point of business inputs faces three pitfalls: determining tax preferences, factor inputs, and tax incidence.\(^{244}\) The relative contribution of each of the three varies widely for different business types and where the state adds more layers of complexity to the measurement process.

*Tax preferences:* Tax preferences are exclusions, exemptions, and deductions from the tax base.\(^{245}\) Each of these seven western states incorporates a wide range of tax preferences. For example, purchases of raw materials are exempt from the

\(^{236}\) Id. at 67 (showing the combined taxes on oil and gas and mining firms in the states compared).

\(^{237}\) N.M. STAT. ANN. §§ 7-9-2, -4 (Michie 2001); but see Proposed GR&CTA Food Credit, supra note 59.

\(^{238}\) See BBER, supra note 225, at 6.

\(^{239}\) See Proposed GR&CTA Food Credit, supra note 59.

\(^{240}\) See BBER, supra note 225, at 75.

\(^{241}\) See pyramiding discussion supra, section III.A.3. The gross receipts tax, unlike sales taxes imposed in other states, taxes the sale of services as well as goods.

\(^{242}\) Id.

\(^{243}\) Id.

\(^{244}\) Id.

\(^{245}\) TAX POLICY IN THE 21ST CENTURY 315 (Herbert Stein ed., 1998).
gross receipts tax in all seven states, while purchases of capital equipment by non-manufacturers are only taxed in California and New Mexico.\textsuperscript{246}

\textit{Factor inputs}: Valuing input purchases is necessary to estimate the taxes paid by representative firms.\textsuperscript{247} The impact of gross receipts/sales taxes without specific information about what, how much, and where firms produce and purchase cannot be assessed. All seven states treat goods similarly. These states all exclude the taxation of goods sold in the manufacturing-distributing process, but they treat services quite differently.\textsuperscript{248}

\textit{Tax incidence}: Tax incidence is a measure of who bears the actual burden of the tax, regardless of who is legally required to remit payment.\textsuperscript{249} There are three ways a sales tax can be paid: (1) forward shifting from the seller to the buyer, (2) backward shifting from the buyer to the seller, and (3) splitting, where both the seller and the buyer share the tax burden.\textsuperscript{250} Splitting can also entail shifting the burden from the consumer to labor, capital, or both.\textsuperscript{251}

These three issues pose difficult obstacles when researching the impact of the gross receipts tax because the necessary information is not available. Tax incidence constantly fluctuates with changes in the national and local economies. Firms facing significant competition are more likely to absorb all or a portion of the tax than they are to raise the price and pass it on to the consumer. Meanwhile, firms selling products or services in high demand are likely to pass the entire tax along. Location also creates differences in the tax incidence because of the effects of local economies.\textsuperscript{252}

Tracing tax preferences also presents complex problems.\textsuperscript{253} New Mexico’s gross receipts tax on the purchase of services is a good example. These services are taxable if they are purchased from businesses in the state.\textsuperscript{254} But, if purchased from an out-of-state firm, the transaction is exempt from the gross receipts tax.\textsuperscript{255} The tax can also be avoided by providing the service in-house.\textsuperscript{256} Information of adequate depth and scope in these areas is simply not available.

\section*{VII. ECONOMIC DEVELOPMENT}

All states offer economic development incentives to businesses. A single state or local government would cease to be competitive if it unilaterally stopped offering such incentives.\textsuperscript{257} There are, however, other reasons for states to offer economic incentives. Incentives can offset aspects of the existing tax system that deter economic growth. For example, a state with very high property or corporate income

\begin{thebibliography}{99}
\item 246. \textit{See} BBER, \textit{supra} note 225, at 75; N.M. STAT. ANN. §§ 7-9-4, 30, -46 (Michie 2001).
\item 247. \textit{See} DAVID C. COLANDER, \textit{ECONOMICS} 11 (1994); BBER, \textit{supra} note 225, at 75-76.
\item 248. \textit{See} BBER, \textit{supra} note 225, at 75.
\item 249. \textit{See} Stein, \textit{supra} note 245, at 315.
\item 250. \textit{See} BBER, \textit{supra} note 225, at 75.
\item 251. \textit{Id.}
\item 252. \textit{Id.} at 75-76.
\item 253. \textit{Id.} at 76.
\item 254. N.M. STAT. ANN. § 7-9-4 (Michie 2001).
\item 255. N.M. STAT. ANN. §§ 7-9-4, -7 (Michie 2001).
\item 256. N.M. STAT. ANN. § 7-9-69 (Michie 2001).
\item 257. \textit{See} BBER, \textit{supra} note 225, at 138.
\end{thebibliography}
taxes that fall heavily on capital intensive industries might offer property tax abatements or an industry-specific double-weighted sales factor\textsuperscript{258} in its income apportionment formula to offset these structural characteristics.\textsuperscript{259} Incentives can also mitigate other community-specific disadvantages like distance from market, high land or construction costs, and the need to develop regions suffering from high unemployment or similar issues.\textsuperscript{260}

Proponents believe that incentives provide a variety of benefits like employment, training for unemployed workers, better quality jobs for the existing labor force, higher wages for all workers because of increased demand, increased property values, increased local business profits, and higher state and local tax collections.\textsuperscript{261} Opponents see an increased tax burden on other taxpayers; lower local business profits arising from higher rents and wages; higher local cost of living, particularly for housing; and higher environmental and traffic congestion costs.\textsuperscript{262} The opposing view assumes that the tax base expansion from the economic development does not pay for both the cost of the incentives and the public service requirements of the growing population.

New Mexico offers several enticing economic development incentives. These incentives include Industrial Revenue Bonds, tax credits, corporate income apportionment choices, and gross receipts tax relief. All of these measures are indirect incentives. The state of New Mexico cannot rely on direct economic development expenditures for new or expanding businesses because the state constitution contains an anti-donation clause.\textsuperscript{263} In 1994, however, New Mexico voters passed a constitutional amendment allowing local governments to provide qualifying businesses with free land and buildings and up to five percent of their general fund for infrastructure improvements.\textsuperscript{264}

A. Industrial Revenue Bonds (IRBs)

The theory behind an IRB is quite simple. If a business wishes to construct a facility within a local community, the normal process for the business would be to purchase the land and construct the facility. Under this scenario, the business, the owner of the land, must pay property taxes on the value of the real property as improved by the facility.\textsuperscript{265} IRBs allow qualifying landowners to avoid this property tax as well as some of the gross receipts or compensating taxes that would be imposed on the purchase of equipment installed in the building.

Usually, when a business is expanding or coming into a new area, it purchases or leases land and hires a contractor to construct its facilities. When a business qualifies

\textsuperscript{258} See double-weighted sales discussion supra, section III.

\textsuperscript{259} See BBER, supra note 225, at 138. For example, Texas offered Intel a two-year moratorium of the state's property tax, but after Intel failed to build within the allotted time, Texas lawmakers declined to extend the tax holiday.

\textsuperscript{260} Id.

\textsuperscript{261} Id.

\textsuperscript{262} Id.

\textsuperscript{263} For example, Industrial Revenue Bonds covered in the next section provide companies with tax incentives to build or expand in New Mexico. N.M. CONST. art. IX, § 14.

\textsuperscript{264} N.M. CONST. art. IX, § 14.

\textsuperscript{265} N.M. STAT. ANN. § 7-36-7, 14, -15 (Michie 2001).
for IRBs, the local government, rather than the business owner, steps in and purchases the land and hires the contractor. The IRB proceeds pay for the land, construction, and equipment. As the legal owner of the real property and the purchaser of the equipment, the local government is exempt from property taxes and from any gross receipts taxes related to purchase of certain equipment. Because the bond purchasers fund the IRBs, the local government is not obligated to use its full faith and credit to back the bonds. Moreover, the business is often the purchaser of the IRBs. For IRBs, the local government is only liable on the bonds to the extent of the rental income from the property. The local government leases the facility to the business and charges enough rent to pay the bonds.

IRB financing aims tax relief at newly locating or expanding businesses. This prevents the state from losing substantial revenue, which is what would otherwise happen if the state exempted all equipment from the GR&CT. By using IRBs, the state only loses GR&CT equipment revenue on new or marginal projects.

The lack of consistent, long-range, statewide data makes it difficult to evaluate the economic incentive effects of IRBs. There is no quantitative accounting by cities or counties of the total amount of outstanding IRB approvals and the state has no IRB reporting requirements. Without central reporting, it is impossible to track the total amount of approved IRBs. It is also difficult to know the effects of IRBs without more information on their fiscal impact.

Without a system to track the total amount of approved IRBs as well as their costs and benefits the state will never know the overall effect of these incentives. In its December 1997 report to the Revenue Stabilization and Tax Policy Committee, the Legislative Council Service included the results of a study on the fiscal impact of IRBs. The Service based its findings on a $29 million dollar Albuquerque project. The report concluded that over the twenty-year life of the bonds, the state general fund would have a tax gain of $38.2 million and Albuquerque would enjoy a tax gain of $4.4 million. While this limited study provided valuable information, its findings are too narrow to decide the debate.

B. Tax Credits

New Mexico offers an investment tax credit equal to the compensating tax rate (currently five percent) on the purchase price of qualified equipment used in a manufacturing operation in New Mexico. The taxpayer must own the equipment. If the taxpayer does not own the equipment, the United States or the state or the local government may own the equipment and lease or sublease it to the

266. N.M. STAT. ANN. § 7-9-54 (Michie 2001); See BBER, supra note 225, at 142.
267. See BBER, supra note 225, at 139.
268. Id.
269. See id. at 142.
270. See id.
271. See id. at 139.
272. NEW MEXICO LEGISLATIVE COUNCIL SERVICE, INDUSTRIAL REVENUE BOND IMPACT STUDY 55 (1997).
273. Id. at 57.
274. Id. at 57-60.
275. N.M. STAT. ANN. § 7-9A-5 (Michie 2001); see Chavez, supra note 50, at 15, 16.
276. N.M. STAT. ANN. § 7-9A-5 (Michie 2001); see BBER, supra note 225, at 142.
taxpayer.\(^{277}\) This allows manufacturing equipment purchased by a local government with IRBs and leased back to the taxpayer to qualify for the credit.

The credit, which is limited to eighty-five percent of taxes due, can be claimed against withholding taxes or gross receipts taxes, including gross receipts taxes on construction.\(^{278}\) The taxpayer, however, can only claim the credit against future tax liabilities and is not entitled to a refund of tax already paid.\(^{279}\) State distributions of gross receipts tax to local governments are sheltered from this credit because the credit only applies to state tax obligations.\(^{280}\)

Furthermore, the credit is only available to businesses that meet an employment requirement.\(^{281}\) For every $250,000 of qualified equipment up to $2 million the taxpayer must have one full time employee on the payroll.\(^{282}\) For equipment values over $2 million, the employment requirements decrease relative to the value of the qualified equipment.\(^{283}\) The employment requirement exists to prevent rewarding manufacturers who replace workers with new equipment. Until 2011, there is no limit on the amount of equipment eligible for the credit.\(^{284}\)

The goal of the investment tax credit is to help New Mexico manufacturers compete nationally.\(^{285}\) Most states either do not impose, or specifically exempt, the gross receipts or compensating tax on equipment purchases by manufacturers.\(^{286}\) States that impose a gross receipts tax and do not specifically exempt manufacturing equipment also provide a similar credit.\(^{287}\)

In its original form, the investment tax credit was a way to rebate the compensating tax paid by New Mexico manufacturers on their capital equipment purchases.\(^{288}\) The 1991 amendment that broadened the credit to include IRB funded purchases transformed the credit into a subsidy for IRB equipment.\(^{289}\) It is similar to a subsidy because those purchases are already exempt from the gross receipts and compensating taxes but are still eligible for the credit anyway.

The investment tax credit has become a relatively expensive economic development program for New Mexico. In 1989 the total investment credit granted was $268,184, which equaled an average cost of $4470 per job.\(^{290}\) Claims accelerated after the 1991 amendment allowed IRB equipment to qualify for the credit.\(^{291}\) By fiscal year 1995, the annual claims were $29.8 million or $44,833 per job.\(^{292}\)

\(^{277}\) N.M. STAT. ANN. § 7-9A-5 (Michie 2001); see BBER, supra note 225, at 142.
\(^{278}\) N.M. STAT. ANN. § 7-9A-8 (Michie 2001); see Chavez, supra note 50, at 15.
\(^{279}\) N.M. STAT. ANN. § 7-9A-8 (Michie 2001); see Chavez, supra note 50, at 15.
\(^{280}\) N.M. STAT. ANN. § 7-9A-8 (Michie 2001); see Chavez, supra note 50, at 15.
\(^{282}\) Id.
\(^{283}\) Id.
\(^{284}\) Id.; see Chavez, supra note 50, at 15.
\(^{286}\) See BBER, supra note 225, at 143.
\(^{287}\) Id. at 148-49.
\(^{288}\) See Chavez, supra note 50, at 15.
\(^{289}\) Id.; N.M. STAT. ANN. § 7-9A-6 (Michie 2001).
\(^{290}\) See BBER, supra note 225, at 143.
\(^{291}\) Id.
\(^{292}\) Id.
In 1999, the state expanded the manufacturer investment tax credit to include the capital equipment tax credit for call centers, businesses engaged principally in taking inbound telephone calls initiated by consumers for the purpose of obtaining goods or services.\textsuperscript{293} The credit applies to call centers that locate or expand to rural areas.\textsuperscript{294} Similar to the investment credit, businesses can take the call center credit against any gross receipts, compensating, or withholding tax due the state.\textsuperscript{295} Qualifying equipment must be used for taking inbound calls, or recording or processing messages.\textsuperscript{296} Unlike the original investment credit, some or all of the credit must be repaid if the center closes down or the equipment is moved within forty-eight months of credit approval.\textsuperscript{297} Moreover, the credit cannot be used against IRB purchased equipment.\textsuperscript{298}

In 2000, the private research and development industry also became eligible for tax credits.\textsuperscript{299} Taxpayers conducting qualified research at a facility in New Mexico may claim a basic credit equal to four percent of qualified expenditures.\textsuperscript{300} These taxpayers may also claim an additional credit of four percent of qualified expenditures if they increase their payroll by $75,000 annually for every $1 million in qualified expenditures,\textsuperscript{301} such as rent, facility operation, maintenance, equipment, software, payroll, and technical manuals and materials.\textsuperscript{302} Both the basic and the additional credits apply against the taxpayer’s gross receipts, compensating, or withholding taxes.\textsuperscript{303} The additional credit may also be claimed against income taxes.\textsuperscript{304} The credit doubles if the qualified facility is in a rural area and includes a recapture provision similar to that in the call center credits.\textsuperscript{305}

C. Multi-State Income Apportionment

At the beginning of 1993, New Mexico gave multi-state corporations the option to change the way they apportion their corporate income.\textsuperscript{306} Before 1993, New Mexico apportioned income using a three-factor formula using sales, payroll, and property located in New Mexico as a percentage of the total corporate sales, payroll, and property.\textsuperscript{307} The state weighted each factor equally.\textsuperscript{308} Corporations may now choose to double the weight for the sales factor.\textsuperscript{309} This gives sales one-half weight and payroll and property one-quarter weight. The change enables export-oriented

\textsuperscript{293} N.M. STAT. ANN. § 7-9D-2 (Michie 2001).
\textsuperscript{294} N.M. STAT. ANN. § 7-9D-4 (Michie 2001).
\textsuperscript{295} N.M. STAT. ANN. § 7-9D-7 (Michie 2001).
\textsuperscript{296} N.M. STAT. ANN. § 7-9D-5 (Michie 2001).
\textsuperscript{297} N.M. STAT. ANN. §§ 7-9A-1 to -11; 7-9D-8 (Michie 2001).
\textsuperscript{298} N.M. STAT. ANN. § 7-9D-5 (Michie 2001).
\textsuperscript{299} See Chavez, supra note 50, at 16; N.M. STAT. ANN. § 7-9F-2 (Michie 2001).
\textsuperscript{300} N.M. STAT. ANN. § 7-9F-5 (Michie 2001).
\textsuperscript{301} N.M. STAT. ANN. § 7-9F-6 (Michie 2001).
\textsuperscript{302} N.M. STAT. ANN. § 7-9F-9 (Michie 2001).
\textsuperscript{303} Id.
\textsuperscript{304} Id.
\textsuperscript{305} N.M. STAT. ANN. §§ 7-9F-8, -11 (Michie 2001).
\textsuperscript{306} See Chavez, supra note 50, at 29.
\textsuperscript{307} N.M. STAT. ANN. §§ 7-4-1, -11, -14, -16 (Michie 2001).
\textsuperscript{308} Id.
\textsuperscript{309} N.M. STAT. ANN. § 7-4-10 (Michie 2001).
corporations with a small percentage of in-state sales to reduce their state income tax liability.

The double-weighted sales option is now available in many states. Arizona and Oregon, other states that have been able to attract high-tech manufacturers, also offer the double-weighted sales formula for apportioning corporate income.\textsuperscript{310} Colorado has a two-factor weighting system that uses only sales and property.\textsuperscript{311} Texas, whose franchise tax is really a corporate income tax, only allows a single-factor sales formula in its income apportionment scheme.\textsuperscript{312}

\textbf{D. Gross Receipts Relief as an Economic Incentive}

In 1992, the state legislature provided a deduction for gross receipts earned from WATS (Wide Area Telephone Service) 800 numbers and certain private communication services in order to attract telecommunication services to New Mexico.\textsuperscript{313} This has proven to be a successful tax incentive. Southwest Airlines Reservation Center, Trace-Miller Technologies, MCI, Taco Bell, and America Online all added or expanded telemarketing or back office accounting centers in New Mexico after this credit was enacted.\textsuperscript{314}

In 1995, New Mexico made the two-year experimental forty-percent deduction for receipts from the sale of jet fuel permanent.\textsuperscript{315} The deduction had originally been part of an economic incentive plan designed to reduce the cost to Southwest Airlines of making Albuquerque a hub.\textsuperscript{316} Southwest’s call center also benefits from the telecommunications deductions enacted in 1992.\textsuperscript{317} Eclipse Aviation has benefited from a new deduction enacted in 2000 for receipts from refurbishing, remodeling, or otherwise modifying transport aircraft weighing over 65,000 pounds.\textsuperscript{318}

In 1998, the year before it provided an investment credit for telecommunications call centers, the legislature enacted “Sprint’s Deduction.”\textsuperscript{319} This initiative expanded the deduction for administrative, accounting, or management services performed by one affiliated corporation or entity for another.\textsuperscript{320} As its name implies, this law helped Sprint reduce its state tax liability.

\textbf{E. Limits on Tax Incentives as Economic Development Tools}

Most states place a cap on the dollar value of many tax incentives.\textsuperscript{321} These caps limit the fiscal impact on state and local governments and make the fiscal impact more predictable for revenue estimating purposes.\textsuperscript{322} In New Mexico, neither the

\begin{footnotesize}
\begin{enumerate}
\item See BBER, supra note 225, at 8, 144.
\item Id. at 144.
\item Id.
\item See Chavez, supra note 50, at 9.
\item Id.; N.M. STAT. ANN. § 7-9-69 (Michie 2001).
\item See BBER, supra note 225, at 151, 152.
\item Id.
\end{enumerate}
\end{footnotesize}
Investment Credit Act nor the IRB program has limits.\textsuperscript{323} Thus, the state's lost gross receipts/compensating tax on manufacturing equipment is both unlimited and unmeasurable.

Furthermore, most states do not provide a one-hundred percent property tax abatement like New Mexico does,\textsuperscript{324} and many states only provide these abatements for limited periods of time.\textsuperscript{325} Additionally, those states that allow some form of property tax abatement require all affected local governments (cities, counties, and school districts) to approve the abatement.\textsuperscript{326} In New Mexico, only the local government that issues the IRB makes the final determination, and the other affected local government organizations are not formally involved in the IRB approval process.\textsuperscript{327}

VIII. TAKING ANOTHER LOOK

As New Mexico enters the twenty-first century, citizens are questioning whether its tax system is truly serving the state well. Voices clamor for reform, but the proposed reform measures are not all the same. Indeed, many times they are mutually exclusive. One group advocates a greater use of tax incentives, while another lobbies for a more comprehensive tax system with fewer breaks. The tension over the state's tax policy leads to an important question: can there be a dispassionate source of information about tax policy or unbiased recommendations for change? As it stands, New Mexico does not have a single voice proposing the design and structure of the state's tax system.

We end this article by "taking another look," and describing some of the choices that are available to the state. These choices are presented as options to be discussed, not as conclusions to be adopted. The first obvious choice for change is to redesign New Mexico's entire tax system. This choice, however, raises a number of crucial issues: What is the balance among the different taxes (gross receipts, personal income, corporate income, property, severance, and other selected taxes) that New Mexico should seek to achieve? If the new system is to be viable, this balance must necessarily consider the tax principles with which we began this report: adequacy, equity, simplicity, and efficiency. To this list of principles we also add economic development—the use of the tax system as a tool to help grow New Mexico's economy. Our first step in looking at the future is to consider the different choices for each of the major taxes. This analysis allows us to understand New Mexico's overall tax system choices.

A. Gross Receipts and Compensating Tax Act

Any look at New Mexico's taxes must begin with the GR&CTA. Its importance cannot be overstated. The GR&CTA raises $1.6 billion for the general fund; this is forty-one percent of New Mexico's total general fund revenues. Any erosion of the

\textsuperscript{323} N.M. STAT. ANN. §§ 7-9A-1 to -11; 3-32-1 to -16; 4-59-1 to -16 (Michie 2001).
\textsuperscript{324} See BBER, supra note 225, at 152.
\textsuperscript{325} Id.
\textsuperscript{326} Id.
\textsuperscript{327} N.M. STAT. ANN. §§ 3-32-6.1, 4-59-4.1 (Michie 2001).
GR&CTA tax base will significantly impact New Mexico’s general fund revenues. Since fifty percent of general fund revenues finance public education, any reduction of the GR&CTA tax base will mean a substantial reduction of funding of public education at a time when support of public education is the primary initiative of the legislature and the governor.

These are the trade-offs that must be considered when reviewing proposals for the removal of the gross receipts tax on services, food, medical services, or other “necessities.” They must also be remembered when proposals for additional tax deductions and exemptions are proposed as incentives to certain industries to locate in New Mexico. Consideration must be given to alternative revenue sources to replenish the lost tax revenue.

At this time, New Mexico could reduce the present breadth of the gross receipts tax base by replacing it with a retail sales tax and an increase in property taxes. A retail sales tax is different from a gross receipts tax in two principal ways. First, the taxpayer is the buyer, not the seller, as is the case with the gross receipts tax. Second, only consumer transactions, not business transactions, are the subject of a sales tax.

The advantages of a retail sales tax are the elimination of direct pyramiding, which removes the economic disincentives that exist in the GR&CTA, and the apparent incidence of the tax. The disadvantages are that under a retail sales tax transactions with the federal government could not be taxed. Since the taxpayer is the buyer, the federal government would be the person who would legally bear the tax, and the state cannot constitutionally tax the federal government. Thus, to replace the revenues lost from business transactions and transactions with the federal government, the tax rate under a retail sales tax would be extremely high, approximately twelve percent. Lastly, unless the retail sales tax is comprehensive and covers the sale of all goods and services, equity and simplicity problems will arise. Similarly situated taxpayers will be treated differently, and definitional problems (for example, what food items are excluded or what are necessities) would result in new and difficult compliance and enforcement issues.

B. Corporate Income Tax

Many economists believe that theoretically the corporate income tax should be repealed. The incidence of the tax (who actually bears the burden) is uncertain, except we know that the corporation itself does not bear the tax. Consumers, labor, suppliers, and/or owners ultimately pay the tax. This incidence problem creates issues of fairness and disincentive.

The second problem with the corporate income tax is that many, but not all, corporations can easily avoid it. Consequently, the tax becomes unfair for those corporations without the market advantages or sophistication for tax planning. On the other hand, repeal of the corporate income tax would cause approximately $161 million of revenue loss. That loss would have to be replaced by another revenue source.
C. Property Tax

New Mexico’s property tax is an enigma. Of all the tax bases in New Mexico, it is probably the one with the greatest capacity for taxation. However, any attempt to increase property taxes will generate widespread public and political reaction against that attempt. Historically, New Mexicans have not favored the property tax because of abuses in the administration and enforcement of the property tax system and because families who have owned land for generations often do not have the wherewithal to pay the tax. This is especially true in Santa Fe and Taos, where values for all property owners have increased with the purchase of high-cost properties by individuals moving into the state.

The changes in the current method of assessing property that accompany any property tax increase are equally important. Although the valuation process is statutory, the implementation of that process differs throughout the state. County assessors do not apply the statutory rules uniformly, and some counties tax property at much higher rates than other counties. Furthermore, tax assessors do not have access to current sales data of property that would allow them to assess property at current values.

D. Limitations on Economic Development Incentives

New Mexico provides businesses with a large array of incentives, and there are proposals to expand the pool. In addition to the questions of equity raised by these incentives, the state’s inability to measure their costs is a serious concern. The purpose of any incentive is to encourage economic growth that results in additional taxes. We presently assume that the benefits from new and additional taxation outweigh the costs of lost tax revenue resulting from these incentives. But we do not actually know whether the benefits exceed the costs of the incentives.

Perhaps New Mexico should require greater reporting and analysis of the costs and benefits and consider more performance standards (i.e., the number of jobs and an increase in the amount of money invested in New Mexico). The state could also place a cap on the total incentives any one business could receive. This cap could be an absolute dollar amount, or it could have some relationship to the amount of growth directly attributed to the business. These choices offer the opportunity to provide some middle ground between those who favor incentives and those who do not. Those who oppose incentives because they doubt that the benefits to the state outweigh the costs might be more willing to accept additional or different incentives if reliable data showed the state received a net benefit.

E. New Mexico Tax Policy

As originally conceived, the New Mexico tax structure was an integrated system in which both the separate tax acts and the system as a whole implemented a comprehensive tax policy. In recent years, the notion of an overall tax policy has been lost. With a reemergence of tax policy, New Mexico should also seek a better balance in its taxes. For example, a tax such as the severance tax or gross receipts tax reacts negatively to market conditions; another tax can plug, or at least slow, the revenue drain. Achieving this kind of balance requires us to consider the state’s
capacity to impose different taxes and to document the consequences of relying on one tax rather than another.

What many states have that New Mexico lacks is an accepted institution that could provide an independent and nonpartisan look at New Mexico's tax system, that could develop an overall tax policy, and that could make recommendations for implementing that policy. The establishment of such a body has been recommended for many years. The creation of a tax commission, however, leads to the questions of where it would be located and how it would be funded. A tax policy commission could be created to review New Mexico's tax system both for its policy and practical ramifications, to provide unbiased assessments of its effectiveness and burdens, and to propose enhancements to New Mexico's tax laws.
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**Table 1: U.S. and New Mexico Economic Indicators**

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**Labor Market and Income Data**

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<td>5.1</td>
</tr>
<tr>
<td>US Personal Income Growth (%)</td>
<td>5.3</td>
<td>5.1</td>
</tr>
<tr>
<td>US Wage &amp; Salary Growth (%)</td>
<td>5.0</td>
<td>4.7</td>
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<tr>
<td>US Private Wages &amp; Salaries Growth (%)</td>
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**New Mexico**

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<tr>
<th>Indicator</th>
<th>Actual</th>
<th>Estimated</th>
</tr>
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<tr>
<td>NM Non-Agricultural Employment Growth (%)</td>
<td>2.2</td>
<td>2.0</td>
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<td>NM Personal Income Growth (%)</td>
<td>5.3</td>
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<td>NM Wage &amp; Salary Growth (%)</td>
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<td>NM Private Wages &amp; Salaries Growth (%)</td>
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**Crude Oil and Natural Gas Outlook**

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<th>Estimated</th>
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<tr>
<td>Oil Price ($/bbl) Gross Sales Value</td>
<td>$22.00</td>
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<tr>
<td>Taxable Oil Sales (million barrels)</td>
<td>74.4</td>
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<tr>
<td>Gas Price ($/ thousand cu. Feet) Gross Value</td>
<td>$2.46</td>
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<tr>
<td>Taxable Gas Sales (million cu. Feet)</td>
<td>1,619</td>
<td>1,552</td>
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*CPI is all Urban, Overnight Yield is the Federal Funds Rate.
Table 2
GENERAL FUND CONSENSUS REVENUE ESTIMATES

<table>
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<th></th>
<th>FY00 Actual</th>
<th>FY01 Estimated</th>
<th>FY 02 Estimated</th>
<th>FY 03 Estimated</th>
<th>FY 04 Estimated</th>
<th>FY 05 Estimated</th>
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<tr>
<td><strong>Dollars in Millions</strong></td>
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<td>General and Selective Sales Taxes</td>
<td>$1,415.10</td>
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<td>$1,581.80</td>
<td>$1,654.80</td>
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<td>$1,801.10</td>
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<td>$1,126.00</td>
<td>$1,187.50</td>
<td>$1,258.90</td>
<td>$1,334.30</td>
<td>$1,414.10</td>
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<td>$336.70</td>
<td>$286.80</td>
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<td>$221.10</td>
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<td>Other</td>
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<td>$79.90</td>
<td>$81.80</td>
<td>$84.40</td>
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<tr>
<td>Total Recurring Revenue</td>
<td>$3,373.50</td>
<td>$3,849.50</td>
<td>$3,903.00</td>
<td>$4,022.10</td>
<td>$4,181.90</td>
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<td>$3,854.50</td>
<td>$3,903.00</td>
<td>$4,022.10</td>
<td>$4,181.90</td>
<td>$4,349.90</td>
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<td>Annual Change Excluding Oil and Gas</td>
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<td>171.6</td>
<td>191.0</td>
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<td>188.7</td>
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**Change Vs. Prior Year**

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<th>FY 02</th>
<th>FY 03</th>
<th>FY 04</th>
<th>FY 05</th>
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<tr>
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<td>6.0%</td>
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<tr>
<td>Mining Taxes</td>
<td>46.4%</td>
<td>73.1%</td>
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<td>-13.0%</td>
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</tr>
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<td>Rents, Royalties and Bonuses</td>
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<td>-11.6%</td>
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</tr>
<tr>
<td>Other</td>
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<td>2.4%</td>
<td>3.1%</td>
<td>3.2%</td>
<td>2.8%</td>
</tr>
<tr>
<td>Total Recurring Revenue</td>
<td>8.0%</td>
<td>14.1%</td>
<td>1.4%</td>
<td>3.0%</td>
<td>4.0%</td>
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</tr>
<tr>
<td>Non-recurring</td>
<td>-1.7%</td>
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<td>0.0%</td>
<td>0.0%</td>
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<td>Grand Total Revenue</td>
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<tr>
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<td>4.0%</td>
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<tr>
<td>Annual Change Excluding Oil and Gas</td>
<td>6.3%</td>
<td>5.5%</td>
<td>5.8%</td>
<td>5.4%</td>
<td>5.1%</td>
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*Detail may not add to column totals due to independent rounding.*
Table 3
PERCENT OF STATE-LOCAL TAX COLLECTIONS BY STATE
GOVERNMENTS FOR FISCAL YEAR 1996

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<th>Rank</th>
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Table 4

STATE AND LOCAL SALES TAX LOSSES FROM ALL REMOTE SALES 2000
($ in millions)

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<th>Rank</th>
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<th>High Estimate</th>
<th>Average</th>
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<tr>
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<td>TOTAL</td>
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Table 5
STATE AND LOCAL SALES TAX LOSSES FROM ALL REMOTE SALES, 2003
($ in millions)

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| TOTAL | $7,111       | $26,402      | $16,757     |

Chart 1

SOURCES AND USES OF THE GENERAL FUND

(in millions)

<table>
<thead>
<tr>
<th>Source</th>
<th>Amount (in millions)</th>
<th>Percentage</th>
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<tbody>
<tr>
<td>Income Taxes</td>
<td>$1,187</td>
<td>30%</td>
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<tr>
<td>General / Selective Sales Taxes</td>
<td>$1,582</td>
<td>41%</td>
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<tr>
<td>Severance Taxes, Rents, &amp; Royalties</td>
<td>$586</td>
<td>15%</td>
</tr>
<tr>
<td>Interest Earnings</td>
<td>$466</td>
<td>12%</td>
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<tr>
<td>Fees, Misc. Receipts, and Reversions</td>
<td>$82</td>
<td>2%</td>
</tr>
<tr>
<td>Public Safety</td>
<td>$259</td>
<td>7%</td>
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<tr>
<td>Higher Education</td>
<td>$582</td>
<td>15%</td>
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<tr>
<td>*Primary and Secondary Education</td>
<td>$1,796</td>
<td>47%</td>
</tr>
<tr>
<td>Health and Human Services</td>
<td>$782</td>
<td>21%</td>
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<tr>
<td>General Government</td>
<td>$375</td>
<td>10%</td>
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Total Recurring General Fund Revenue: $3,903

Recommended Expenditures FY02

Total Recommended General Fund Expenditures: 3,794

Difference between Revenue and expenditures: $75 Tax Reduction; $20 Other; $14 to Reserves