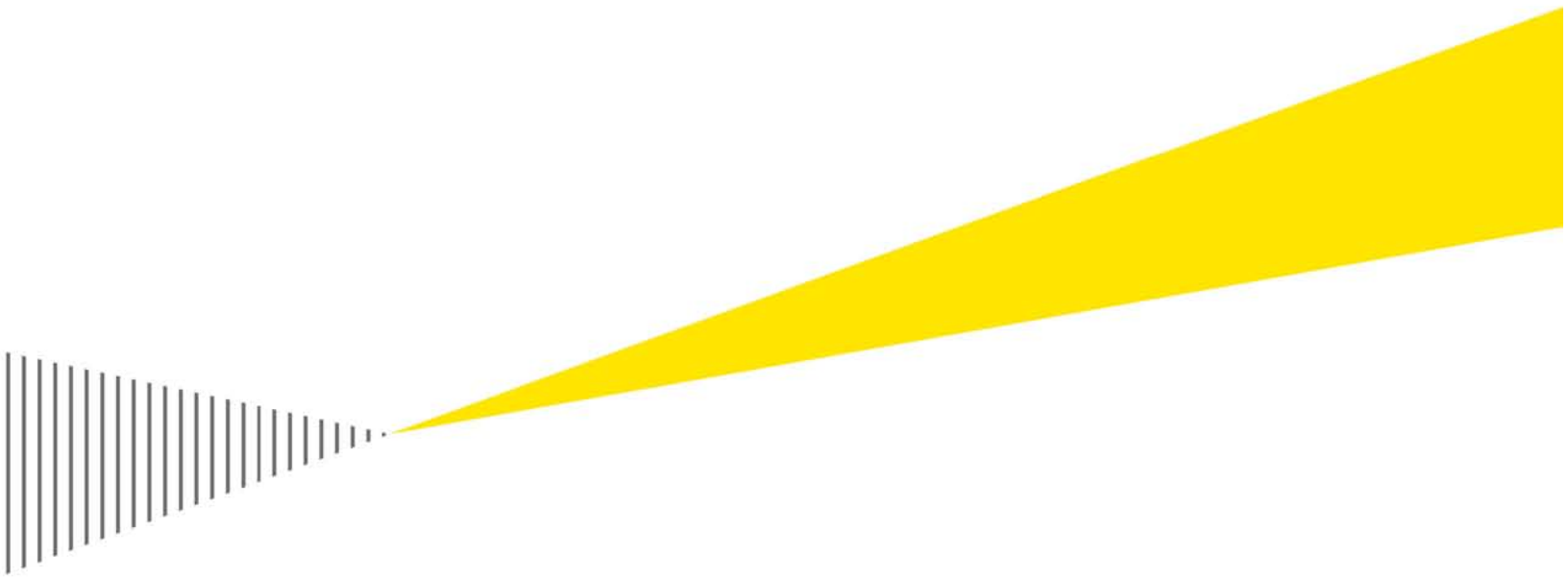
New Mexico Business Tax Competitiveness Study: Updated Results

Prepared for the New Mexico Tax Research Institute

January 2014



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EXECUTIVE SUMMARY FROM NEW MEXICO TAX RESEARCH INSTITUTE

2014 NEW MEXICO BUSINESS TAX COMPETITIVENESS STUDY UPDATE

INTRODUCTION

Forward

The 2011-2012 Business Tax Competitiveness Study was a collaborative effort whereby the State of New Mexico, the City of Albuquerque, Bernalillo County, the New Mexico Municipal League and seven private sponsors funded the New Mexico Tax Research Institute ("NMTRI") to engage Ernst & Young, LLP to expand upon a recently completed 50 state study on effective state tax rates for certain modeled business. That study centered on a hypothetical $100 million dollar investment by corporations in nine different industries. The corporations in the study were assumed to export 95% of their respective goods and services, and were assumed to be subject to corporate income tax.

The 2011 New Mexico Business Tax Competitiveness Study compares eight other states with New Mexico -- Arizona, California, Colorado, Nevada, Oklahoma, Oregon, Texas, and Utah. The states' tax rates were compared before and after the inclusion of existing tax credits and incentives offered by each state. For purposes of determining local property tax rates, the study assumed the business location would be in Albuquerque. Another set of results was calculated using Deming, New Mexico to reflect the differing tax and incentive structures presented by rural communities. Industry sectors studied include – headquarters, research and development, office and call center, durable manufacturing, non-durable manufacturing, computer and electronic manufacturing, electrical equipment and aerospace products and parts, management scientific and technical consulting, and food processing.

Commonly discussed policy options were also modeled in order to get an idea of how they would impact effective tax rates of the hypothetical corporate investments. These scenarios included:

(1) reducing the New Mexico corporate tax rate to 4.9%;
(2) allowing corporate income tax apportionment by single or double weighted sales factor;
(3) eliminating the gross receipts tax on manufacturing "consumables"; and
(4) allowing a tax increment incentive similar to one recently adopted in Utah.

The results of the study showed that while New Mexico had the highest effective tax rate for all industry categories before existing incentives were taken into account, after incentives were accounted for, New Mexico's ranking improved significantly in several categories, in some cases to the most competitive of all states modeled. The 2011 study can be found on the New Mexico Tax Research Institute website here: http://www.nmtri.org/associations/3740/files/New%20Mexico%20Business%20Tax%20Competitiveness%20Study%202012.pdf

Subsequent events

Things have changed. The earlier study, based on one performed by Ernst & Young, LLP for the Council on State Taxation, incorporated tax rates in effect in 2009. This 2014 update incorporates the most recent state and local tax rates (effective 12/2013). This is important because since 2009, tax rates in New Mexico and elsewhere have changed. For instance, the state gross receipts tax rate was subsequently increased (.125% to 5.125% before local option taxes are added), and mill levies in Bernalillo and Luna counties have gone up as well. Accordingly, New Mexico's effective tax rates on the modeled businesses have gone up without consideration of other more recent legislative changes. Tax rates in the other modeled jurisdictions have also changed.

And there have been recent legislative changes. Legislation was passed in the 2012 and 2013 legislative sessions and signed into law by the governor directly impacted the effective tax rates of the modeled companies. The 2012 legislation found in House Bill 246 eliminated gross receipts tax on some manufacturing inputs and consumables. That elimination is being phased-in over a five year period in 20% increments, beginning July 1, 2013. That same legislation also reduced some "pyramiding" of gross receipts tax in the construction industry. The 2011 and 2014 studies do not consider the negative effects of excessive pyramiding in New Mexico's gross receipts tax beyond taxation of direct business inputs, so any potential decrease in the effective tax rate (ETR) presented by the changes to construction related gross receipts tax (GRT) were beyond the scope of this study. *Note: the impacts of pyramiding on effective tax rates to businesses and households are certainly worthy of further and future study.*

The 2013 legislation found in House Bill 641 had several provisions that will impact the effective tax rates for the modeled companies. The legislation:

- Reduced corporate tax rates from 7.6% to 5.9%;
- Provided a single sales factor election for manufacturers who apportion business income to New Mexico;
- Both narrowed and expanded the GRT "consumables" deduction passed in the 2012 session (the former not impacting the ETR calculation as the narrowing impacted businesses outside the scope of this study);
- Narrowed the scope and increased qualifying wage thresholds of the High Wage Jobs Tax Credit ("HWJTC"); and
- Provided authority for municipal and county governments to each increase GRT rates in 1/8 increments up to 3/8%.

The legislation also made changes to the state's film production credit, required certain retailers to file on a combined basis in certain cases for purposes of the corporate income tax, and repealed "hold harmless" payments to local governments over a fifteen year period. Neither of the first two provisions impact the modeled companies or their respective ETR calculations; however, the latter was the impetus for the expanded local government rate authority that does have the potential to impact modeled ETRs.

Time to Re-evaluate

While some of the tax law changes of recent legislative sessions were modeled in the 2011 report, and some ETR changes could be inferred from that work, years have passed and New Mexico as well as the other states have or are implementing changes. Policy makers and those interested in economic development began asking questions once again on how New Mexico compares.

The New Mexico Tax Research Institute engaged Ernst & Young to update the 201-2012 study to account for changes in tax laws and rates in New Mexico and the competing states. For purposes of comparability, representative company profiles were left unchanged. Tax law changes that were being phased-in over a period of years were assumed to be fully phased-in, both in New Mexico and other states (i.e. Arizona). Since New Mexico provided additional rate imposition authority in 2013 to allow local governments the flexibility to offset some or all of the negative impacts of the repeal of the "hold harmless" distribution to local governments, the question of whether some sort of GRT rate increase should be assumed over present law rates to account for the additional authority was raised. Many local governments may not impose additional increments at all or may wait many years to do so. (Again, the hold harmless phase out doesn't begin until 2015 and occurs over a 15 year period and only one local government, the Village of Corrales, has imposed higher rates as a result of the additional authority.) But, it was decided that erring on the conservative side was better than not assuming any rate increase at all. Since 2/8% of the allowed 3/8% municipal imposition and 1/8% of the allowed 3/8% county imposition was sufficient to keep most municipal and county governments "whole" from a budgetary perspective, the combined 3/8% was assumed to be imposed in addition to present law New Mexico GRT rates.

Results

The results are anything but shocking. Most of the business favorable tax policies enacted in the last several years were targeted toward the manufacturing sectors, which saw significant decreases in effective tax rate despite increases in gross receipts and property tax rates as well as a higher threshold for the High Wage Jobs Tax Credit. On a comparative basis, New Mexico now presents the lowest effective tax rates to three of the four hypothetical company investments in manufacturing sectors, and the second lowest ETR in the fourth. Interestingly and counter to the historic trend, the bulk of the additional effective rate reduction achieved in the manufacturing sectors since the prior study now occurs pre-incentive rather than post. (Recall that New Mexico had the highest effective tax rate in all studied sectors before the application of incentives.)

Non-manufacturing ETR's faced the same headwind as the manufacturing sectors in terms of the increasing GRT and property tax rates, as well as increased wage thresholds for the High Wage Jobs Tax Credit (HWJTC). However, the only change reducing ETR's in the non-manufacturing sectors was the decrease in corporate income tax rates.

Analysis Before and After Existing Incentives Are Taken Into Account

After existing incentives were taken into account, relative rankings for New Mexico by broad and narrow sectors were as follows:

Change in effective tax rates 2011 to 2013, before credits,

Average for manufacturers and services

	Manufacturers			Services		
States	**2011**	**2013**	**Percent Change**	**2011**	**2013**	**Percent Change**
Arizona	6.9%	5.8%	-15.1%	10.3%	8.3%	-19.3%
California	6.0%	5.8%	-3.5%	10.2%	9.7%	-4.2%
Colorado	5.8%	6.2%	7.1%	7.7%	8.2%	5.9%
Nevada	6.9%	6.8%	-2.0%	6.9%	6.7%	-2.3%
New Mexico	17.9%	9.5%	-46.9%	13.4%	12.6%	-6.3%
Oklahoma	9.9%	10.0%	1.5%	12.0%	12.4%	3.2%
Oregon	3.5%	3.6%	3.1%	2.3%	2.3%	1.7%
Texas	10.8%	10.9%	1.4%	7.9%	8.1%	2.7%
Utah	6.6%	6.8%	3.0%	6.9%	7.0%	2.8%
Average without NM	*7.0%*	*7.0%*	*-0.7%*	*8.0%*	*7.9%*	*-2.0%*

After existing incentives were taken into account, relative rankings for New Mexico by broad and narrow sectors were as follows:

Change in effective tax rates 2011 to 2013, after credits,

Average for manufacturers and services

States	Manufacturers			Services		
	2011	2013	Percent Change	2011	2013	Percent Change
Arizona	4.4%	4.2%	-4.2%	9.0%	8.0%	-11.8%
California	5.8%	5.6%	-3.6%	9.8%	9.4%	-4.3%
Colorado	5.7%	6.1%	7.2%	7.5%	8.0%	6.0%
Nevada	5.7%	5.6%	-1.8%	6.3%	6.1%	-2.1%
New Mexico	8.1%	3.3%	-59.5%	3.4%	6.1%	81.0%
Oklahoma	9.0%	9.2%	1.7%	12.0%	12.4%	3.2%
Oregon	3.4%	3.5%	3.2%	2.1%	2.2%	1.8%
Texas	10.8%	10.8%	0.6%	7.9%	7.9%	0.0%
Utah	5.5%	5.7%	3.9%	6.5%	6.7%	2.9%
Average without NM	*6.3%*	*6.3%*	*0.9%*	*7.6%*	*7.6%*	*-0.9%*

Change in effective tax rates comparative rankings from the 2011 to 2013 studies, after credits

Industry	NM's Effective Tax Rate (ETR) 2009 rates/2011 study	NM Effective Tax Rate (ETR) 2013 rates
Headquarters	1st Highest	2nd Highest
Research and Development	9th Highest (Lowest)	9th Highest (Lowest)
Renewable Energy Equipment Manufacturing	1st Highest	8th Highest(2nd lowest)
Business Support Services	8th Highest	3rd Highest
Food Products Manufacturing	1st Highest	4th highest
Computer & Electronics Manufacturing	3rd Highest	9th Highest (Lowest)
Electrical Equipment Manufacturing	1st Highest	7th Highest/3rd Lowest
Aerospace Products and Parts Manufacturing	9th Highest (Lowest)	9th Highest (Lowest)
Management, Scientific and Tech. Consulting Services	9th Highest (Lowest)	8th Highest(2nd Lowest)

Background on the Study Original Study

Long-standing concerns about the potentially uncompetitive nature of New Mexico's tax system were brought to a head in 2011 when a large manufacturing operation targeted by local economic development recruitment efforts decided to locate elsewhere, citing tax issues as a major part of the basis for their decision. Specific tax issues identified by the company included the gross receipts tax on manufacturing inputs (electricity in this case) and the absence of a single sales factor option which allows exporters to substantially reduce corporate tax liability.

In response, Mayor Richard J. Berry of Albuquerque convened an informal group of advisors to discuss New Mexico's ability to compete for new capital investment by manufacturers and other mobile capital. Recalling the KPMG Berents Group study from 1997, performed for the state Economic Development Department and the Town of Silver City, it was suggested that rather than simply reacting to the concerns of one company, the issues should be studied in a

comprehensive fashion that took into account all taxes and different industries. The fifteen-year-old KPMG Berents Group study used a "representative firm (or business)" model in which a hypothetical set of financial statements are calculated for each industry reflecting all of their expenses associated with making a large new investment. The tax system of each jurisdiction included in the study is then applied to these hypothetical financial statements to determine each state's effective tax rate on the new investment inclusive of all applicable taxes. The comparison of locations was made before and after tax incentives and credits.

The KPMG Berents Group study ranked New Mexico as having the 3rd highest average overall effective tax rate in seven industry sectors modeled in nine geographic locations before incentives. After including incentives, New Mexico was more competitive with the 5th highest average effective tax rate, demonstrating that New Mexico relied more heavily on credits and incentives to achieve its tax policy objectives than did other compared states.

At the same time Mayor Berry's advisory group was considering commissioning a study, the Council on State Taxation ("COST"), a Fortune 1000 trade association focused on state and local taxes, released a study they had commissioned Ernst &Young LLP's Quantitative Economics and Statistics Practice ("E&Y") to perform. That study, titled *Competitiveness of State and Local Taxes on New Business Investment* modeled the effective tax rate on a hypothetical C-corporation making a hundred million dollar investment in each state and the District of Columbia. Their model assumed investment was made in the largest city of each state for purposes of property tax rates, and used the statewide average sales tax rate (which coincidentally was almost exactly Albuquerque's tax gross receipts tax rate). That study looked at five sectors: headquarters facilities, research and development facilities, office and call center facilities, durable manufacturing facilities, and non-durable manufacturing facilities, but did not include the impact of economic development incentives. The study showed New Mexico ranked 51st in terms of how it taxed new corporate investments--that is, it had the highest effective tax rate on the investments modeled. The study made the following explicit reference and commentary regarding New Mexico:

> *For the selected facility types, New Mexico's state and local business tax system imposes the greatest tax burden of any state, reducing the rate of return by an average 16.9%. This relatively high tax burden results from several factors:*
>
> - *New Mexico uses an equally weighted corporate income apportionment formula. New Mexico's formula apportions to the state a share of national income equal to the average of the percentage of the taxpayer's nation-wide sales, payroll and property in the state. For the hypothetical facilities, this means that roughly two thirds of the additional income attributable to the new investment will be subject to tax in New Mexico. In addition, New Mexico's corporate tax rate is slightly above average (7.6% in New Mexico compared to a nation-wide average of 6.7%).*
>
> - *New Mexico imposes a gross receipts tax on virtually all business activity. The tax is levied at a relatively high tax rate for a gross receipts tax (5.125% at the state level) plus a local tax comparable to retail sales taxes. However, unlike a retail sales tax, it applies to most services. While this tax is technically a liability of the seller, in practice it is passed forward to purchasers and is typically stated separately on invoices. Therefore, this analysis treats the tax as a sales tax with few exemptions, resulting in a significant tax burden for facilities that purchase a large amount of*

services and other inputs typically exempt from state and local sales taxes. In sharp contrast to New Mexico, Ohio, ranked the 4th most competitive state, imposes a gross receipts tax at a rate of 0.26%.

- *New Mexico taxes both real and tangible personal property, although the property tax rate in Albuquerque is slightly below average. The business tax competitiveness index shows the large difference in business tax burdens among the states. Based on the ETRs presented in Table 2, the average state and local business tax burden in the 10 most competitive states (5.0%) is only 42% as large as the average tax burdens for the 10 least competitive states (11.8%). The results also show that more than 20 states have business tax burdens that vary in the narrow range of 6% to 8%.*

A clear limitation of the E&Y/COST study was its failure to include incentives. For instance, Texas would have been given credit in the study for their sales tax exemption for manufacturing equipment, but New Mexico was not given credit for its investment tax credit, which essentially does the same thing. New Mexico is also a difficult state to model in this type of study, given its unique tax structure. While it can be argued that the results are more accurate for businesses not eligible for incentives, most new investments of the magnitude and in the industry sectors modeled are typically eligible for tax incentives and credits.

The Mayor's group decided that for reasons of expediency and cost, it made sense to leverage the fresh work of Ernst & Young while attempting to address the shortcomings of its initial study. The New Mexico Tax Research Institute was commissioned by the City of Albuquerque and Bernalillo County, as well as the New Mexico Taxation and Revenue Department, Economic Development Department, Department of Finance and Administration, and Legislative Finance Committee to engage Ernst & Young and direct and coordinate an enhancement of the initial study.

Mayor Berry also solicited and received significant private sector financial support from National Association of Industrial and Office Properties, Public Service Company of New Mexico, New Mexico Municipal League, Greater Albuquerque Chamber of Commerce, Southwest Multiple Listing Service, Inc., Greater Albuquerque Association of Realtors, Sheet Metal and Air Conditioning Contractors Association, and the Mechanical Contractors Association of New Mexico. The enhanced study added industry sectors, a more rural location (Deming, NM), and modeled frequently discussed policy options.

Strengths, Limitations and Other Caveats

Representative business comparisons such as this one have the benefit of holding all variables constant so that a direct comparison of relative tax burden among differing tax jurisdictions can be made. While the approach provides an "apples-to-apples" comparison of tax burden on given investments and operations, the reality is all other variables are not constant. New Mexico might compare favorably or unfavorably relative to cost of labor, real estate, utilities or other non-tax business costs that could outweigh the tax expense associated with a given investment. Accordingly, tax burdens are not the only considerations in business expansion, location, and

relocation decisions. However, when all other things are held equal, tax burdens can be very significant and certainly factor into investment decisions.

Since this study is an enhancement of the broader Ernst & Young study, it is limited to the assumptions made in that original study. For a more detailed description of the underlying model and assumptions, that study can be found at:

http://cst.informz.net/z/cjUucD9taT0xNDQ4NTYxJnA9MSZ1PTEwMDIzNjc2NzEmbGk9NjI5NTAyMw/index.html.

For more background, the 1997 KPMG Barents Group Study can be found on the NMTRI website at:

http://www.nmtri.org/associations/3740/files/KPMG Berents Group NM Tax Study.pdf.

The study necessarily makes relatively simple corporate income tax assumptions and does not model the effects of combined reporting mandated by other states versus New Mexico's separate filing option. Also, while the study accounts for the tax burden on business inputs, it does not attempt to model the effects of pyramiding in the supply chain inside or outside of New Mexico. New Mexico's broad gross receipts tax base when combined with relatively high rates results in more pyramiding of tax than other states' sales tax structures, increasing the cost of purchasing goods and services in New Mexico relative to others states. As previously mentioned, other offsetting costs such as potentially lower costs of labor or real estate are also not modeled in this study.

Changes in assumptions can yield dramatic changes in results as well. For instance, corporate income tax is a significant driver of New Mexico's effective tax rate on the modeled industry sectors. If a similar investment were made by a company not taxed as a corporation (general partnerships, S-Corporations, LLPs, LLCs, etc.) the results would change meaningfully for both New Mexico and comparison states.

The study is not an all-encompassing view of tax burden on static large businesses, small businesses, households or the like – all of which would be worth studying. This study is merely a piece of a larger puzzle focusing on the tax impacts on large corporate capital investment.

Policy Options, Tradeoffs, and Recommendations

Policy makers who want to reduce New Mexico's tax burden on new corporate investment in sectors where New Mexico still ranks highest can see from the results of this study how the policy options modeled would reduce that burden. In fact, any tax reduction or incentive that offsets taxes due will reduce effective tax rates. Any decision on whether to implement these or other similar options, however, will require consideration of general tax policy objectives, as well. For instance, reducing the effective tax rate imposed on a manufacturer of goods for export could be accomplished in one of several ways--using targeted tax credits, eliminating any tax on inputs, reducing corporate or gross receipts tax rates, or changing corporate income apportionment factors (like the single-weighted sales factor), etc. Each of those options presents different broader tax policy implications to the state's overall tax structure, not to

mention differing fiscal impacts to state and possibly local government revenue. If the primary concern is the exporter's effective tax rate, a narrowly crafted solution that minimizes the fiscal impact might suffice. Alternatively, broader reform can be accomplished with tax rate reduction or broader revisions to the tax code, but this is a more costly way to lower the effective tax rate for a given sector. While narrower options may be less costly, they may also be seen as less certain and less equitable. Most tax policy issues and options present tradeoffs and conflicts between good tax policy principles. Still, the New Mexico Tax Research Institute attempts to view and evaluate tax policy within the context of such principles. Those principles endorsed by our organization are reprinted after the acknowledgments, and we hope you take the time to read them.

Acknowledgments

The New Mexico Tax Research Institute wishes to thanks those that contributed in large and small ways to the study and without who's financial and other support, this effort would not have been possible. The effort was exemplary of good government and non-partisan public/private sector collaboration-- something New Mexico should continue to pursue. (If we left anyone out, we apologize.)

From New Mexico State Government

The Hon. Susana Martinez, Governor, State of New Mexico

Thomas E. Clifford, PhD, Secretary, Department of Finance and Administration

John Barela, Secretary, Economic Development Department

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From City of Albuquerque:

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From the New Mexico Legislature

Senator John Arthur Smith, Chairman, Legislative Finance Committee

David Abbey, Director, Legislative Finance Committee

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Generous Community Support

Albuquerque Economic Development

Albuquerque Economic Forum

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New Mexico Municipal League

New Mexico Partnership

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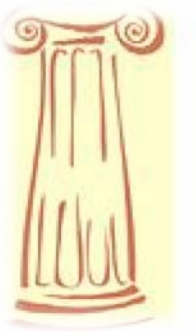
Southwest Multiple Listing Service, Inc.



Principles of the New Mexico Tax Research Institute

It's important, particularly when dealing with tough economies, tough decisions, and the emotionally charged subject of taxes, to view the world in the context of principles. Taxes are good in that they raise the money we need to pay for the services we want. They're bad in that they often create inefficiencies, distortions, and sometimes inequities. A more rational approach is to look at our entire tax system rather than getting "lost in the weeds" focusing only on a particular rate or some item we choose to tax or not tax. Taxes should raise the amount of money needed (and there's obviously plenty of debate to be had on that subject) while doing the least harm to the economy, allowing for job creation, promoting fair treatment of taxpayers and protecting the most vulnerable. Accordingly, we've taken the opportunity to reprint our principles of good tax policy here:

State and local taxes should be adequate to provide an appropriate level of those goods and services best provided by the public sector, such as education, public safety, law enforcement, streets and highways, and the courts.

- State and local tax policy should do the least harm to the private economy. Therefore, tax bases should be as broad as possible so that tax rates can be as low as possible in order to raise the necessary revenues.

- State and local tax policy should be fair and equitable towards individuals and businesses similarly situated. Individuals with the same income level should be taxed the same. Businesses engaged in similar commercial activities should be subject to the same level of taxation.

- State and local tax policy should not be costly to administer and should be easily understood by taxpayers so as to minimize taxpayer compliance costs.

- The state and local tax burden should be evaluated on the basis of the impact of all taxes levied on a given taxpayer, not just a single tax or tax rate.

- Deviations from established tax policy in pursuit of economic development, social or other goals should be well-reasoned and pursued only when established tax policies are not significantly undermined and the results of such deviations can subsequently be measured and evaluated.

New Mexico Business Tax Competitiveness Study: Updated Results

Prepared for the New Mexico Tax Research Institute

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New Mexico Business Tax Competitiveness Study: Updated Results

This analysis presents updated estimates of the competitiveness of New Mexico state and local business taxes prepared for the New Mexico Tax Research Institute in 2011.[1] The updated estimates compare effective state and local tax rates (taxes divided by pre-tax income) in New Mexico and selected other states between 2011 and 2013. The effective tax rates (ETRs) are modeled for representative new business investments in nine industries. The 2013 ETRs incorporate fully phased in tax features, including tax rates and corporate income tax apportionment formulas, in current law at the end of the 2013 state legislative sessions.

In New Mexico, current law includes business tax changes adopted in both the 2012 and 2013 legislative sessions. The New Mexico changes included:

- A 22.4% reduction in the statutory corporate income tax rate (from 7.6% to 5.9%)
- Substantial reductions in the percentage of manufacturing inputs subject to the gross receipts tax
- A shift to a single sales factor corporate income tax apportionment formula for manufacturers
- A reduction in the value of the "high-wage" jobs tax credit through a 50% increase in the minimum salary necessary to qualify as a high-wage job.
- A phase out of the state's obligation to make "hold harmless" payments to local governments in exchange for a local option to raise local sales tax rates. The local option will allow counties and municipalities to increase the local rate up to a maximum of 0.375%.[2]

[1] *New Mexico Business Tax Competitiveness*, report prepared by EY (December 2011). See the prior report for a detailed description of study methodology and the taxes and industries included in the analysis.

[2] Although it is unclear how much local governments will actually increase the local rates, the ETR calculations assume that the combined rate for counties and municipalities will, on average, increase by 0.375%. To the extent that the combined local sales tax rate is increased by less than 0.375%, the estimated general reductions in New Mexico ETRs will be even larger. It should also be noted that any increases in local sales tax rates are expected to occur over a longer time period than the state business tax changes.

A number of tax changes also occurred between 2011 and 2013 in the other states that are compared to New Mexico. These include:

- Arizona adopted substantial reductions in state and local business taxes over this period. When fully phased in, the changes will reduce taxes on the included manufacturing investments by 15.1%, on average, and taxes on the service industries by 19.3%, a fairly uniform, across-the-board set of business tax reductions.

- Business taxes in California and Nevada were reduced by 2% to 5% between 2011 and 2013; in both states, the reductions were uniform across all industry examples.

The study calculates both before-credit and after-credit effective tax rates.[3] Key results of the updated study (summarized in Tables 1a and 1b) include:

- The New Mexico law changes reduced state and local taxes before-credits for the five manufacturing examples by *46.9%*, on average. When calculated after tax credits, the tax rate decrease for manufacturers is even greater, nearly 60%.

- While the New Mexico manufacturing ETR before-credits is still one-third higher than the average for the other included states (Arizona, California, Colorado, Nevada, Oklahoma, Oregon, Texas and Utah), it fell from a level that was over 2.5 times as high as the average to 35.7% higher than average; New Mexico's before-credit average manufacturing rate is now *lower* than the rate in Oklahoma and Texas.

- New Mexico's average manufacturing ETR after credits fell from 8.1% to 3.3% and is now the lowest in the region. At 3.3%, New Mexico's rate is 48% lower than the regional average of 6.3%.

- For the four service industry examples, New Mexico's law changes reduced the average ETR before credits by *6.3%* due to the corporate income tax reduction that was partly offset by higher local tax rates. New Mexico still has the highest average, before-credit ETR for services of all the included states with Oklahoma as a close second.

- The average New Mexico ETR after credits for the service industry examples increased from 3.4 to 6.1% due to the reduction in the high-wage job credit that

[3] The study includes statutory credits available to general taxpayers. These include investment tax credits, wage credits and research and development credits. The analysis does not include discretionary (negotiated) tax credits.

more than offset the benefits of the lower corporate income tax rate. New Mexico's average after-credit ETR for services is still relatively low compared to the other states in the study. With the changes between 2011 and 2013, New Mexico's average has changed from 55% below the average in other states in 2011 to 20% below the average in 2013.

- The calculations show that the average manufacturing tax rate, before credits, in the other included states declined by only 0.7% from 2011 to 2013. The average service industry before-credit ETR in the other states dropped by 2%.

Changes in Effective Tax Rates: 2011 to 2013

Table 1a compares average effective tax rates in 2011 and 2013 for the five manufacturing examples and the four service industry examples included in the competitiveness analysis before tax credits are taken into account. Table 1b shows the same comparison on an after-credit basis.

A comparison of ETRs in Tables 1a and 1b show that the 2013 changes in New Mexico's credit programs have different impacts on the effective tax rates for manufacturers and services taxpayers. The 2013 change increased the minimum salary necessary for a job to qualify for the high-wage jobs tax credit, resulting in a reduction in the size of the credit. Under the new law, a salary must be at least $60,000 in order to qualify for the high-wage jobs tax credit, whereas earlier the minimum salary was $40,000.

The change in the minimum salary requirement had relatively large impacts on the ETRs for service companies. For example, approximately 83% of persons employed in the R&D industry qualified for the tax credit in the 2011 study, but only 48% qualify for this credit in the updated 2013 study. The high-wage jobs credit change reduced the credit significantly for this industry. While the credit change reduces the amount of the credits for both manufacturers and services, it results in a relatively larger reduction for the service industry examples. The combination of a relatively small reduction in the before-credit services ETR and the relatively large reduction in the credit offset, results in a large percentage increase in the average after-credit ETR for the service company examples.

A comparison of the ETRs in Tables 1a and 1b, highlights the significant progress that New Mexico has made over the last several years in creating a much more competitive state and local business tax structure for manufacturers. At the same time, the results show that the reduction in the high-wage credits in 2013 that apply to both manufacturers and service providers increased the after-credit ETRs for selected service companies compared to the 2011 levels.

Table 1a
Change in effective tax rates 2011 to 2013, before credits,
Average for manufacturers and services

	Manufacturers			Services		
States	2011	2013	Percent Change	2011	2013	Percent Change
Arizona	6.9%	5.8%	-15.1%	10.3%	8.3%	-19.3%
California	6.0%	5.8%	-3.5%	10.2%	9.7%	-4.2%
Colorado	5.8%	6.2%	7.1%	7.7%	8.2%	5.9%
Nevada	6.9%	6.8%	-2.0%	6.9%	6.7%	-2.3%
New Mexico	17.9%	9.5%	-46.9%	13.4%	12.6%	-6.3%
Oklahoma	9.9%	10.0%	1.5%	12.0%	12.4%	3.2%
Oregon	3.5%	3.6%	3.1%	2.3%	2.3%	1.7%
Texas	10.8%	10.9%	1.4%	7.9%	8.1%	2.7%
Utah	6.6%	6.8%	3.0%	6.9%	7.0%	2.8%
Average without NM	*7.0%*	*7.0%*	*-0.7%*	*8.0%*	*7.9%*	*-2.0%*

Table 1b
Change in effective tax rates 2011 to 2013, after credits,
Average for manufacturers and services

	Manufacturers			Services		
States	2011	2013	Percent Change	2011	2013	Percent Change
Arizona	4.4%	4.2%	-4.2%	9.0%	8.0%	-11.8%
California	5.8%	5.6%	-3.6%	9.8%	9.4%	-4.3%
Colorado	5.7%	6.1%	7.2%	7.5%	8.0%	6.0%
Nevada	5.7%	5.6%	-1.8%	6.3%	6.1%	-2.1%
New Mexico	8.1%	3.3%	-59.5%	3.4%	6.1%	81.0%
Oklahoma	9.0%	9.2%	1.7%	12.0%	12.4%	3.2%
Oregon	3.4%	3.5%	3.2%	2.1%	2.2%	1.8%
Texas	10.8%	10.8%	0.6%	7.9%	7.9%	0.0%
Utah	5.5%	5.7%	3.9%	6.5%	6.7%	2.9%
Average without NM	*6.3%*	*6.3%*	*0.9%*	*7.6%*	*7.6%*	*-0.9%*

Changes in Before-Credit ETRs

Table 2 provides more detailed information comparing the change in ETRs by state between 2011 and 2013 for the nine industry examples. The changes are calculated before any state business tax credits. The ETRs show how competitive the New Mexico business tax system would be in the absence of statutory tax credits. The table shows that the combined impact of the 2012 and 2013 business tax changes ranges from a cut of 3.7% for the business support services to a 51.1% reduction for renewable

energy equipment manufacturing. The very large reductions for manufacturing are accounted for by the single sales factor apportionment for manufacturers, the corporate income tax rate reduction, and the elimination of gross receipts taxes on a significant portion of business input purchases. The service sectors do not qualify for the single sales factor apportionment or the gross receipts tax reduction.

Changes in After-Credit Effective Tax Rates

Table 3 shows the impact of statutory tax credits, by industry, in reducing business effective tax rates. The first block of the table presents the before-credit ETRs for combined state and local business taxes by industry and state. In addition to the ETRs, the table also ranks the states in terms of ETRs with 1 being the state with the highest ETR.

The middle block of Table 3 shows the estimated reduction in before-credit ETRs due to state credits. For example, the results show that state tax credits reduce New Mexico's effective tax rate on electrical equipment manufacturing by 4.8 percentage points, a 46% reduction in the before-credit ETR.

The final block shows the ETR after subtracting the impact of credits. For example, the after-credit New Mexico ETR for electrical equipment manufacturing is 5.6% (before-credit ETR of 10.4% plus the ETR reduction due to credits of -4.8%). Among the comparison states, New Mexico ranks between second highest (for headquarters) and lowest (for research and development, computer and electronics manufacturing, and aerospace manufacturing) in terms of after-credit ETRs.

Table 2
Change in effective tax rates 2011 to 2013, by state and industry, before-credits

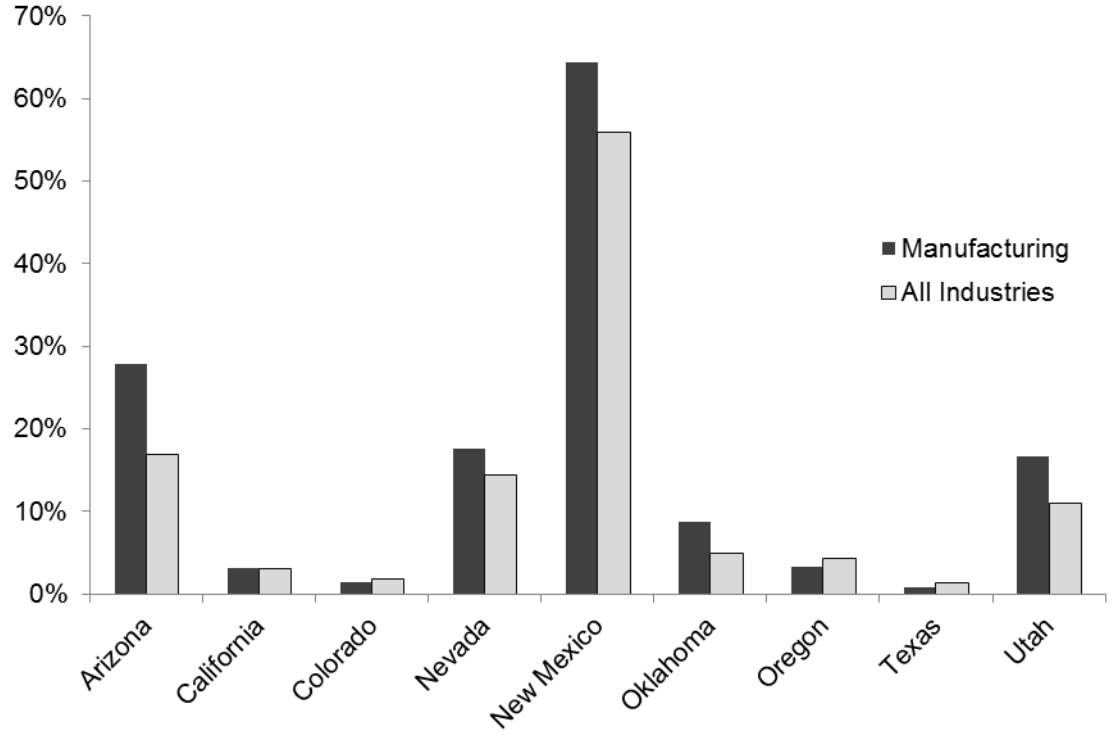
State	Renewable Energy Equipment Manuf.	Food Product Manuf.	Computer & Electronics Manuf.	Electrical Equipment Manuf.	Aerospace Products and Parts Manuf.	Headquarters	Research & Development	Business support services	Management, scientific, and technical consulting services
Arizona	-16.2%	-16.5%	-17.4%	-10.9%	-15.2%	-58.1%	-14.4%	-18.6%	-20.6%
California	-3.6%	-3.4%	-3.8%	-2.9%	-3.7%	-1.6%	-3.7%	-4.5%	-4.3%
Colorado	7.3%	6.8%	6.6%	7.5%	7.2%	4.3%	6.2%	5.6%	6.0%
Nevada	-2.2%	-2.1%	-1.8%	-1.7%	-2.3%	-1.0%	-1.7%	-2.6%	-2.3%
New Mexico	-51.1%	-45.4%	-50.9%	-48.5%	-39.9%	-20.8%	-7.8%	-3.7%	-4.1%
Oklahoma	1.2%	1.0%	2.3%	1.4%	1.6%	0.3%	2.6%	3.9%	3.7%
Oregon	3.1%	3.1%	3.0%	3.2%	3.2%	1.2%	1.8%	1.3%	2.4%
Texas	1.0%	0.8%	1.9%	1.5%	1.5%	2.3%	2.4%	2.7%	2.8%
Utah	2.7%	2.9%	2.6%	3.4%	3.3%	2.4%	2.8%	2.7%	3.0%
Average without NM	*-0.8%*	*-0.9%*	*-0.8%*	*0.2%*	*-0.6%*	*-6.3%*	*-0.5%*	*-1.2%*	*-1.2%*

Table 3
State and local effective tax rates by industry and state, before and after credits, 2013

State	Renewable Energy Equipment Manufacturing		Food Products Manufacturing		Computer and Electronics Manufacturing		Electrical Equipment Manufacturing		Aerospace and Defense Manufacturing		Headquarters		Research and Development		Business Support Services		Management, Scientific, and Technical Consulting Services	
Total State and Local Taxes	ETR	Rank	ETR	Rank	ETR	Rank	ETR	Rank	ETR	Rank	ETR	Rank	ETR	Rank	ETR	Rank	ETR	Rank
Arizona	4.9%	7	4.6%	7	6.1%	7	6.8%	6	6.7%	6	0.5%	5	8.8%	4	14.6%	4	9.3%	6
California	5.1%	6	4.6%	8	6.6%	5	6.1%	8	6.6%	8	0.7%	3	9.3%	3	17.6%	3	11.5%	3
Colorado	4.7%	8	6.8%	3	5.9%	8	6.7%	7	6.7%	7	0.5%	4	8.0%	6	14.6%	5	9.6%	4
Nevada	7.1%	4	6.3%	5	6.4%	6	6.9%	5	7.4%	5	0.2%	9	6.1%	8	12.4%	8	8.2%	7
New Mexico	8.6%	2	8.4%	1	7.4%	3	10.4%	3	12.7%	2	3.9%	2	11.2%	2	19.3%	1	15.8%	1
Oklahoma	8.8%	1	8.1%	2	10.4%	1	10.4%	2	12.3%	3	4.4%	1	11.7%	1	18.7%	2	14.7%	2
Oregon	3.1%	9	3.3%	9	2.4%	9	4.8%	9	4.3%	9	0.5%	6	4.3%	9	3.4%	9	1.2%	9
Texas	8.0%	3	6.6%	4	10.3%	2	13.3%	1	16.4%	1	0.4%	8	8.5%	5	14.0%	6	9.5%	5
Utah	5.9%	5	5.7%	6	7.4%	4	7.3%	4	7.7%	4	0.5%	7	7.3%	7	12.7%	7	7.8%	8
Average without NM	*6.0%*		*5.7%*		*7.0%*		*7.8%*		*8.5%*		*1.0%*		*8.0%*		*13.5%*		*9.0%*	
Less Tax Credits																		
Arizona	-1.5%	8	-1.5%	8	-1.1%	8	-1.6%	8	-2.2%	8	0.0%	1	-0.6%	5	-0.7%	6	-0.1%	5
California	-0.2%	4	-0.1%	4	-0.2%	4	-0.2%	4	-0.2%	4	0.0%	1	-0.7%	7	-0.6%	5	-0.2%	7
Colorado	-0.1%	3	-0.1%	3	-0.1%	2	-0.1%	1	-0.1%	1	0.0%	7	-0.4%	4	-0.4%	3	-0.1%	4
Nevada	-1.2%	7	-1.1%	7	-0.9%	6	-1.3%	7	-1.5%	7	0.0%	8	-1.0%	8	-0.8%	8	-0.6%	8
New Mexico	-5.5%	9	-2.9%	9	-6.4%	9	-4.8%	9	-11.3%	9	-0.2%	9	-8.2%	9	-4.5%	9	-12.8%	9
Oklahoma	-0.9%	5	-0.9%	5	-0.6%	5	-0.7%	5	-1.2%	6	0.0%	1	0.0%	1	0.0%	1	0.0%	1
Oregon	-0.1%	2	-0.1%	1	-0.1%	3	-0.1%	2	-0.2%	3	0.0%	1	-0.4%	3	-0.2%	2	-0.1%	3
Texas	-0.1%	1	-0.1%	2	-0.1%	1	-0.1%	3	-0.1%	2	0.0%	1	-0.2%	2	-0.5%	4	-0.1%	2
Utah	-1.1%	6	-1.0%	6	-1.1%	7	-1.1%	6	-1.1%	5	0.0%	1	-0.7%	6	-0.7%	7	-0.1%	6
Average without NM	*-0.7%*		*-0.6%*		*-0.5%*		*-0.6%*		*-0.8%*		*0.0%*		*-0.5%*		*-0.5%*		*-0.2%*	
Total State and Local Taxes after Credits																		
Arizona	3.4%	7	3.1%	9	5.0%	7	5.2%	8	4.5%	7	0.5%	5	8.2%	4	13.9%	5	9.2%	5
California	4.9%	4	4.4%	7	6.4%	3	5.9%	5	6.4%	5	0.7%	3	8.6%	2	17.0%	2	11.3%	2
Colorado	4.6%	6	6.7%	2	5.9%	5	6.6%	3	6.6%	3	0.5%	4	7.7%	5	14.1%	4	9.5%	3
Nevada	5.9%	3	5.1%	5	5.6%	6	5.6%	6	5.8%	6	0.2%	9	5.1%	7	11.5%	8	7.6%	7
New Mexico	3.0%	8	5.5%	4	1.0%	9	5.6%	7	1.4%	9	3.7%	2	3.0%	9	14.9%	3	3.0%	8
Oklahoma	7.9%	2	7.3%	1	9.8%	2	9.7%	2	11.1%	2	4.4%	1	11.7%	1	18.7%	1	14.7%	1
Oregon	3.0%	9	3.2%	8	2.3%	8	4.7%	9	4.1%	8	0.5%	6	3.9%	8	3.2%	9	1.1%	9
Texas	7.9%	1	6.5%	3	10.2%	1	13.2%	1	16.3%	1	0.4%	8	8.2%	3	13.4%	6	9.4%	4
Utah	4.8%	5	4.6%	6	6.2%	4	6.2%	4	6.5%	4	0.5%	7	6.6%	6	12.0%	7	7.6%	6
Average without NM	*5.3%*		*5.1%*		*6.4%*		*7.2%*		*7.7%*		*1.0%*		*7.5%*		*13.0%*		*8.8%*	

Figure 1 shows the percentage reduction in the ETRs due to statutory credits for manufacturing as a group and for all industries combined in each state. The figure shows that, relative to the comparison states, New Mexico relies much more on statutory credits to reduce relatively high, before-credit ETRs. In New Mexico the average estimated reduction in ETRs due to statutory credits is to 64.3% for the five manufacturing industries and 55.9% for all the industries combined. In contrast, the average reduction in the other states in the all-industry, before-credit ETR due to statutory credits is 7.2%.

Figue 1
Percentage reduction in ETRs from statutory credits



Effective Tax Rates in Albuquerque and Deming

The final table, Table 4, presents estimates for the changes in ETRs if the new investments are made in Albuquerque and Deming.[4] Table 4 compares the ETRs by industry for Albuquerque and Deming, both before and after credits. Deming has a property tax rate that is 50% lower than Albuquerque; this is offset by a local gross receipts tax rate that is nearly 25% higher in Deming. The net result is slightly lower before-credit ETRs in Deming for the investments included in the study.

In addition, the investments in Deming qualify for more generous high-wage jobs tax credits. The combination of lower before-credit ETRs and larger tax credits on the same investments that were made in Albuquerque results in substantially lower overall ETRs in Deming. Manufacturers located in Deming receive an average reduction of 8.4% in their pre-credit ETRs as compared to 6.2% in Albuquerque. The services industries receive an average reduction of 9.4% in Deming verses a 6.4% reduction in Albuquerque. Manufacturing and service industries have an average ETR of 0.2% and 3.2%, respectively in Deming; in Albuquerque manufacturing and service industries have an average ETR of 3.3% and 6.1%, respectively.

[4] The Albuquerque local tax rates for property taxes and gross receipts taxes, as well as the city's credit rates and provisions, were used in the calculation of statewide ETRs in the prior tables. Therefore, the Albuquerque ETRs shown in Table 4 are equal to the statewide ETRs.

Table 4
Comparison of Albuquerque and Deming ETRs - before and after credits, 2013

I. Taxes before credits	Renewable Energy Equipment Manufacturing	Food Products Manufacturing	Computer and Electronics Manufacturing	Electrical Equipment Manufacturing	Aerospace and Defense Manufacturing	Headquarters	Research and Development	Business Support Services	Management, Scientific, and Technical Consulting Services
Total state and local taxes									
Albuquerque	8.6%	8.4%	7.4%	10.4%	12.7%	3.9%	11.2%	19.3%	15.8%
Deming	7.8%	7.7%	6.8%	9.2%	11.7%	3.9%	10.7%	19.7%	16.2%
Corporate/business tax									
Albuquerque	0.3%	0.3%	0.3%	0.3%	0.3%	3.5%	4.0%	4.3%	3.8%
Deming	0.3%	0.3%	0.3%	0.3%	0.3%	3.5%	4.0%	4.3%	3.8%
State sales tax									
Albuquerque	6.0%	5.5%	5.4%	6.6%	9.0%	0.2%	4.7%	11.3%	8.7%
Deming	6.0%	5.5%	5.4%	6.6%	9.0%	0.2%	4.7%	11.3%	8.7%
Property Tax									
Albuquerque	1.9%	1.9%	1.4%	3.0%	2.6%	0.1%	1.5%	0.7%	0.6%
Deming	1.0%	1.0%	0.7%	1.6%	1.4%	0.0%	0.7%	0.4%	0.3%
Local Sales Tax									
Albuquerque	0.4%	0.7%	0.3%	0.6%	0.9%	0.1%	1.1%	3.1%	2.7%
Deming	0.5%	0.9%	0.4%	0.7%	1.1%	0.1%	1.3%	3.7%	3.3%
II. Taxes after credits									
Tax credits									
Albuquerque	-5.5%	-2.9%	-6.4%	-4.8%	-11.3%	-0.2%	-8.2%	-4.5%	-12.8%
Deming	-8.0%	-3.2%	-7.8%	-5.4%	-17.4%	-0.2%	-10.8%	-7.7%	-18.9%
Total state and local taxes after credits									
Albuquerque	3.0%	5.5%	1.0%	5.6%	1.4%	3.7%	3.0%	14.9%	3.0%
Deming	-0.2%	4.4%	-1.0%	3.7%	-5.7%	3.7%	-0.1%	12.0%	-2.7%