

Protecting low-income working families from tax refund lenders

The federal earned income tax credit (EITC) and New Mexico's working families tax credit (WFTC) are some of the best measures for lifting working families and children out of poverty. *But their effectiveness is greatly diminished* by tax refund anticipation loans.

New Mexico's working families received more than \$370 million from the EITC in 2005. New Mexico's WFTC, now worth 10 percent of the federal EITC, is returning \$37 million more to our working families.

Unfortunately, a significant amount of these tax refund dollars is siphoned off by tax refund lenders who charge outrageous fees for providing a refund anticipation loan (RAL).

According to H & R Block's website, a RAL for a \$1,000 refund is \$140

- ✓ That's 14 percent for a *no-risk loan* of about a week!
- ✓ That can amount to more than the *entire WFTC refund amount!*

Such predatory lending practices undermine the good that was intended by lawmakers in passing the WFTC.

In New Mexico, eligible families received the following tax credits in 2005:

New Mexico	
Total number of personal income tax returns	821,707
Number of tax returns with EITC	195,132
EITC amount returned to working families	\$368,267,225
Amount of WFTC at 10 percent (had it been enacted in 2005)	\$36,826,722
Number of tax filers who got a RAL	69816
Number of tax filers with an EITC who got a RAL	48,363

Data Source: Brookings

NM Voices for Children strongly supports legislation that would:

- ✓ Mandate full disclosure of fees, including the APR
- ✓ Place a cap on the amount tax preparers and lenders can charge for RALs

Thank you for your support of the state working families tax credit!

Please preserve this credit for the working families it was intended to help by enacting strong RAL regulation legislation.

✓ *Fair Taxes, Spending, and the Revenue Shortfall*

**When times were good, we cut taxes for higher income New Mexicans;
Now that times are tough, we should not cut services for those who need them the most**

The state personal income tax (PIT) cuts of 2003 delivered the biggest benefits to those in the highest income bracket, while the bottom 40 percent of taxpayers received no benefits at all. This made New Mexico's tax system significantly less progressive – meaning those who earn the most no longer pay a higher percentage of their income in taxes than those who earn the least.

Now, a family starts paying the *top* income tax rate of 4.9 percent when they make just \$22,000. A family making \$100,000 or more also pays 4.9 percent. The 2003 tax cuts are now costing the state \$500 million.

These tax cuts were phased in over a 5-year period, and we even delayed the phase-in for a year when revenue was needed. A partial roll-back of the PIT cuts should be considered instead of cutting services to those most vulnerable in our state – kids, the poor, and the disabled.

Recovering from the Recession

New Mexico does not have a spending crisis; it has a revenue crisis. Finding new revenue must be part of the solution. Economists agree: cutting services is *not* the most effective way of dealing with a recession. Cutting spending on basic services means cutting safety net programs precisely when they are most needed.

President Obama and Congress plan to build a bridge to economic recovery by increasing investments in programs. This will include an increase in the federal Medicaid match rate (known as FMAP). If we cut our own Medicaid spending we will forego substantial funding from the federal government.

A fair tax system should include:

- ✓ Elimination of the tax loophole that allows those who can afford to itemize to deduct state and local taxes paid from their New Mexico taxable income
- ✓ Regulation of tax refund anticipation loans, which allow tax preparers to siphon millions from working families' tax refund checks through high fees
- ✓ Unitary combined reporting, which would require multi-state corporations to pay their share of income taxes

Revenue can be raised by:

- ✓ Rolling back a portion of the 2003 PIT cuts on the highest income New Mexicans
- ✓ Collecting a small surtax on those New Mexicans making over \$200,000 a year
- ✓ Tapping into the state's operating reserve – the so-called "rainy day fund"
- ✓ Decoupling the New Mexico estate tax from the federal one so we can set our own estate tax rate
- ✓ Joining the 18 other states that have disallowed the federal "qualified production activities" (QPAI) tax deduction for businesses, which costs New Mexico an estimated \$13 to \$21 million
- ✓ Reclassifying AlcoPops – flavored alcoholic drinks – as hard liquor so they are properly taxed
- ✓ Reinstating the gross receipts tax (GRT) on soft drinks

Other ways to boost New Mexico's economy that don't cost the state money:

- ✓ Increase the amount of unemployment insurance (UI) benefits
- ✓ Improve state efforts to increase Food Stamp utilization

✓ *Tax Increment Development Districts*

We can't afford to give away hundreds of millions in state revenue to developers when we're facing several more years of budget shortfalls

Our current Tax Increment Development District (TIDD) law has dire consequences for the long-term health of our state's General Fund.

The redirection of state gross receipts tax (GRT) revenues for tax increment financing to greenfield* developers is largely unprecedented – both in New Mexico and across the country.**

The two developments already approved for state TIDD funding will divert more than \$1.1 billion in state gross receipts taxes from the General Fund over the next 25 years. This is a guaranteed revenue stream to developers that is beyond the oversight of the Legislature, and represents more in annual capital outlay funds than each county, except Bernalillo, received in 2008.

Our TIDD law needs to be amended because:

- ✓ It changes the original purpose of tax increment financing (TIF) from encouraging urban revitalization to development of undeveloped or "greenfield" areas.
- ✓ TIDDs shift the costs of on-site infrastructure from the developer to the taxpayer
- ✓ It is being used for developments that need no incentives because they will occur anyway.
- ✓ It circumvents the Legislature's authority and responsibility to appropriate state General Fund and capital outlay money.

TIDDs are risky because:

- ✓ Most of the GRT revenue to be used for TIDDs would otherwise become state general fund revenues to provide education, health, public safety and other critical services for the whole state.
- ✓ There is no ongoing provision for state oversight, even though the majority of the funding will be state revenues.
- ✓ Developers can control the TIDD governing boards, handle procurement outside of normal state guidelines, and set prices for work to be done. This creates many conflicts of interest and provides many opportunities for mismanagement.
- ✓ No mechanisms are in place to track whether TIDDs actually pay for themselves – thus meeting the "no net cost" claim. There is debate about whether TIDDs have paid for themselves elsewhere in the country.

Legislation is needed to:

- ✓ Disallow greenfield developments from using any state GRT as part of tax increment financing
- ✓ Require all TIDDs to meet certain public and community objectives such as affordable housing, water sustainability, and new jobs at fair wages
- ✓ Place a moratorium on new TIDDs in greenfields until the long-term impacts on state revenues can be determined

*'Greenfield' refers to previously undeveloped land.

**Illinois did attempt TIF with state revenues in the 1980s, but an emergency repeal was enacted when it became clear that the state was losing more than \$300 million a year. See Klemens, M.D. (1990, June). "TIFs: What Cost to the State Treasury," Illinois Issues, June 1990. Retrieved October 12, 2007, from Illinois Periodicals Online: <http://131.156.59.13/ipo/1990/ii900618.html>

✓ **Health Care – Cover KIDS FIRST**

Maximizing Medicaid is the most cost-effective way to cover kids and the best way to boost our economy

Covering kids allows us to maximize two federally funded programs – Medicaid and the State Children's Health Insurance Program (S-CHIP) – both of which inject millions into the state's economy, create jobs, keep our health care infrastructure on solid ground, and keep health care costs lower for everyone.

Congress is expanding S-CHIP and raising the federal match (called FMAP) for Medicaid. Medicaid is the vehicle for delivering federal economic recovery money to the states. Cutting back on our Medicaid spending would be like letting the air out of that vehicle's tires.

Economic Impact

While providing health care to our state's most vulnerable children, Medicaid has the added advantage of boosting job creation in the private health care sector.

Current funding for New Mexico Medicaid generates \$3.36 billion in economic activity annually and sustains more than 43,600 New Mexico jobs.*

The economic impact of Medicaid is most important to rural communities, which often have the highest rates of poverty and lowest rates of health insurance coverage, and where hospitals rely on Medicaid funding.

In addition to the economic benefits, Medicaid also helps to contain health care and private insurance costs for everyone. Medicaid also allows people to get preventive and maintenance care, which greatly reduces medical costs down the line.

The Best Investment

Another reason it makes sense to cover kids first is that, by and large, children are relatively inexpensive to cover. While kids make up 59 percent of Medicaid enrollment, they only make up 27 percent of Medicaid expenditures.

In fact, the child coverage portion of Medicaid and S-CHIP combined is less than 4 percent of the state's general fund budget.

Medicaid also benefits the economy in the long term. An investment in a child's health is an investment in New Mexico's future because children learn best when they are healthy and receive regular care. In order to have the best chance for school success, a child must have screenings for vision, hearing, developmental delays, and other issues that can impact learning.

Maximizing Medicaid would:

- ✓ Allow us to enroll eligible children who are not already covered
- ✓ Invigorate the state's health care economy by bringing in more federal dollars
- ✓ Add fuel to an economic engine, especially in rural New Mexico where it's most needed

**NM Voices for Children estimates using IMPLAN software*

✓ *Corporate Tax Reform: Unitary Combined Reporting*

New Mexico is not collecting approximately \$70-\$90 million in corporate income tax revenue every year

New Mexico's tax code allows profitable, multi-state corporations to avoid paying some \$70-\$90 million in corporate income taxes (CIT) every year. These are the same corporations – big-box stores and national chains – that do business and pay income taxes on their profits in neighboring states.

Our tax laws allow multi-state corporations to report their New Mexico earnings in another state, such as Delaware, that doesn't collect CIT. So even though they are profitable here, their New Mexico tax returns don't show that profit.

This not only puts New Mexico small businesses at a disadvantage – it undercuts the state's ability to provide funding for basic infrastructure and services.

The \$70-\$90 million in lost revenue means:

- ✓ The state has to short-change important programs like public safety, education and health care for kids.
- ✓ The rest of us – including New Mexico small businesses – pay for the infrastructure that allows these multi-state corporations to do business here.

Unitary Combined Reporting and Economic Development

Most states do not have this problem because they have a law that requires **unitary combined reporting**, which closes this loophole.*

*Every other state west of the Mississippi River – except Oklahoma – requires unitary combined reporting.***
Our neighboring states that collect these taxes have not found it to be a detriment to economic development.

In 2006, the state Taxation and Revenue Department took Wal-Mart to court, and an \$11.6 million tax assessment against the giant retailer was upheld.

The state has also taken Kmart and Sonic to court over unpaid CITs. But taking corporations to court is an expensive and inefficient way to collect taxes.

In 2003, the Blue Ribbon Tax Commission stated in its final report to the state Legislature that, *"combined reporting is the fairest approach to corporate taxation at the state level."*

Unitary combined reporting legislation would:

- ✓ *Not* hurt our efforts to attract new, multi-state businesses
- ✓ Level the playing field for New Mexico-owned corporations
- ✓ Make profitable multi-state corporations pay their fair share
- ✓ Help bridge coming revenue shortfalls without program cuts that put our kids at risk

*Unitary combined reporting means that multi-state corporations must "combine" the income they earned in every state where they do business (except those that don't require it, like New Mexico). A formula is then used to determine how much CIT the corporations owe to each state.

**Except those states that do not collect CIT.

✓ *Child Care and Early Education*

Parents can work when they can afford child care

One of the best ways to battle a recession is to put people to work. State investments in child care and early education are a critical work support for New Mexico's parents.

The average annual cost for full-time care at a center for a 4-year-old is \$5,382.* That's 25 percent more than the average annual tuition at a 4-year New Mexico state college, which is \$4,260. Child care typically eats up more than a third of a single mother's income.

More than 99,000 New Mexico children under the age of six are in need of child care because their parents must work. Because quality matters, an investment in child care is an investment in New Mexico's future.

Children who receive quality child care and early education:

- ✓ Are less likely to repeat a grade or require special education or child welfare services
- ✓ Are more likely to graduate from high school
- ✓ Are less likely to engage in criminal activity
- ✓ Earn more as adults – making them contributors to society, not drains on it

Legislation should:

- ✓ Keep child care assistance eligibility at 200 percent of the Federal Poverty Level (FPL) without a waiting list
(Child care assistance eligibility was recently restored so that families living at up to 200 percent of the FPL may receive it. Let's keep it there.)

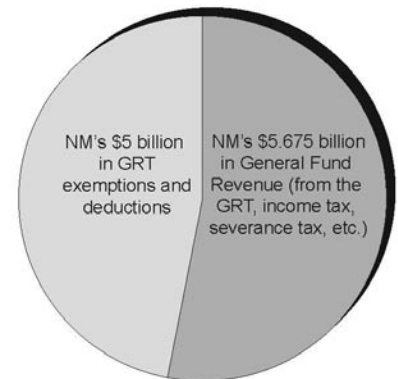
*National Association of Child Care Resource and Referral Agencies: <http://www.naccrra.org/>

Tax Expenditure Reporting

Every year our state decides how much money from the nearly \$6 billion General Fund to spend on each department, project or program. This decision is based in part on how much money was spent in the previous year.

Every year our state also “spends” another \$5 billion on tax exemptions, deductions and credits – known collectively as tax expenditures. While new tax expenditures can be enacted every year, the state does not consider the cumulative effect and revenue losses of all the tax expenditures that have been made over the years.

The state indirectly spends almost as much money on tax expenditures as it does on direct spending for programs and departments. In other words, a complete General Fund revenue picture – one in which all \$11 billion in spending was taken into account – would look like the pie chart to the right.



Aside from not considering the cumulative revenue effect, the state also does not know if the tax expenditures are providing the economic boost they were designed to provide because their impact is never studied.

For example, several years ago the state made some health-care providers exempt from the gross receipts tax in an effort to keep doctors from leaving the state to practice elsewhere. But the state will never know the true fiscal impact of the exemption or even whether it keeps doctors from leaving New Mexico.

Most tax expenditures benefit very limited numbers of people. Some examples of statutory exemption groups are insurance companies, bail bondsmen, racetracks, and boat fuel. Uranium enrichment, lottery retailers, and warranty fulfillment also enjoy deductions. There are even exemptions and deductions for some oil, natural gas and mining activities.

Tax Transparency

A tax expenditure requirement would have the Taxation and Revenue Department create a report every year on how much our tax expenditures are costing and what effect they are having – just like the state's other departments have to create budgets every year that show how much money they are spending and how.

A tax expenditure report would allow our Legislature to review tax expenditures as well as General Fund expenditures. In 2007, the Legislature passed a tax transparency bill, but the governor did not sign it.

In a year when the revenue outlook is slim, doesn't it make sense to take a look at the entire revenue pie, including the half we've decided not to collect?

Tax transparency is good government and it means we're serious about fiscal accountability.