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The Honorable Stephanie Schardin Clarke
Secretary of Taxation and Revenue
P.O. Box 630
Santa Fe NM 87504-0630

Dear Secretary Schardin Clarke:

These comments are submitted for the record at the hearing to be held September 8, 2022 regarding various gross receipts and tax administration rules.

A comment on style. Amending an existing rule by deleting it entirely and then restating all of it with the addition of some actually new material (e.g., 3.2.213.9 NMAC) is undoubtedly easy on the agency. It reduces the work needed to prepare the final rule for submission to the Records Center. It requires more than counterbalancing additional effort on the part of the public, however, because the "new" material must be compared with the deleted "old" material to determine if there are any changes. Since the point of the rule publication process is to make rule changes as transparent as possible—even if it does create more work for the agencies, this style undermines the intent of the State Rules Act.

3.1.1.19C (reimbursed expenditures): Given the 2022 amendment of Section 7-9-3 NMSA 1978 to include a definition of "disclosed agency" that does not include the requirement that the third party have the power to bind the principal, the deletions in Paragraphs (1) through (3) are probably unavoidable. The new definition does change the landscape, perhaps considerably. Apparently all that is required now for an agent's reimbursements to be excluded from the agent's gross receipts is that the third party have knowledge of the agency relationship—whether or not the agent or the principal has affirmatively disclosed it to the third party. How does the agent demonstrate that? Or does the agent simply deduct all "reimbursements" and dare the Department to prove that the third party did *not* have knowledge of the agency relationship?

Throwing out all the existing examples, which are based on prior law, is perhaps justified if none are still valid under the new definition. (But what about Examples 2 and 4?) What is not justified is leaving the taxpayer clueless as to what the new boundaries of "disclosed agency" are. The Department has a reputation for solving problems through litigation; this looks very much like another run down that road.

3.2.106.7A and 3.2.106.15 (cannabis): Do not adopt these proposed rules.

3.2.106.7A declares that cannabis is not an agricultural product. But clearly it is. There was even testimony before the Legislature that legalizing the raising and selling of cannabis would be a boon to a stagnant agricultural sector.

3.2.106.15 declares that receipts from selling cannabis flowers are not receipts from selling unprocessed agricultural products. Flowers of other plants are, so what grounds does the Department have for singling out cannabis flowers for punitive treatment?

In both proposed rules, the Department appears to be exceeding its authority. Neither the Cannabis Regulation Act, the Cannabis Excise Tax Act nor any other act declares cannabis is not an agricultural product. No law gives the Department authority to determine whether or not a plant is an agricultural product. If the tax treatment the Department apparently prefers is to be adopted, it must be by act of the Legislature.

3.2.213.7, 3.2.213.9 & 3.2.213.13 (related to advertising):
In 3.2.213.7A, the expansion of the definition of "regional" seems rational as far as it goes. In a set of rules trying to get its arms around the digital world, it is odd that the definition of "regional" relies on physical presence and does not include businesses with definite on-line (or economic) presence in more than one state. The ***Wayfair*** decision opened the door for such an interpretation.

3.2.213.7C defines "principal place of business". The proposed definition, however, is incomplete because it ignores the digital world. For instance, there are firms that reside solely on laptop computers and do business entirely through the Internet. Under the proposed definition, such outfits would have no principal place of business.

3.2.213.9B brings out an interesting difference between deductions requiring a nontaxable transaction certificate and those that do not. The last sentence of this subsection actually is correct but should it be? Subsection F of Section 7-9-43 NMSA 1978 imposes on the buyer the seller's tax liability when the buyer misuses an NTTC. No part of the Gross Receipts and Compensating Tax Act, however, imposes the seller's tax liability on a buyer for a buyer's violation of the conditions of any non-NTTC-requiring deduction. (One wonders why not since "alternative evidence"—basically the normal type of evidence for non-NTTC-requiring deductions—can substitute for an NTTC.) Section 7-9-7A(2) NMSA 1978 imposes the compensating tax on the buyer if the seller's receipts were not subject to the gross receipts tax. Clearly, if the buyer misled the seller into thinking that the seller could take a deduction, the seller's receipts would not be subject to the gross receipts tax. Compensating tax would be due—but at the rate at the buyer's place of use, not the seller's business location. Given that local option rates apply to compensating tax, there could easily be a difference between what the buyer owes in compensating tax and what the seller would owe in gross receipts tax and which local governments receive the local option tax revenue. It is this sort of mismatch that 7-9-43F NMSA 1978 corrects for NTTC-requiring deductions.

3.2.213.9C is obviously self-contradicting in both its old and new versions; unfortunately, this is a common error in gross receipts rules. It should state: "Receipts from sales of broadcast time by New Mexico radio and television broadcasters to advertising agencies are gross receipts but may be deductible under Section 7-9-48 or 7-9-55 NMSA 1978."

3.2.213.9E simply mirrors 3.2.2139B without, however, discussing NTTCs. If the NTTC rules are the same for digital advertising transactions, why not say so? Also, the last sentence about agency commissions is not only misplaced but also unnecessary since it is plainly stated in 7-9-55C NMSA 1978. (See 14-4-5.7B NMSA 1978.)

3.2.213.13A: Really? Consider an example from the sports world. Professional athletic contests can be viewed on cable television or the Internet. While some (perhaps most) of the advertising is on behalf of national or regional businesses, much of the advertising (particularly for baseball games) will be for merchants or restaurants in the home (or visiting) team's locality. Clearly the target (or as 3.1.4.13C(5)(e)(v) puts it "intended") audience for these advertisements is local. Today, those locations would be entirely outside New Mexico. I think it unlikely that any federal court would uphold New Mexico's claim to a piece of that advertising dollar. The intent here is understandable but I believe some further refinement is required.

3.1.4.13C(5)(e)(v) states that the reporting location for digital advertising services is the location of the server hosting the advertiser's digital platform. OK. But the example also discusses the advertiser's intended viewing audience. So, if the intended viewing audience in wholly within New Mexico, would 100% of the advertising receipts be gross receipts, even if the advertising is viewed by persons elsewhere (say, Hong Kong)? Conversely, if the intended audience is entirely without New Mexico, would no part of the receipts be gross receipts even if some New Mexicans view the message? How will you nail down what the advertiser's intent is?

"Digital platform" is defined in Subsection C, not B, of 3.2.213.13.

Sincerely,

James P. O'Neill