
FYI-270

New Mexico
Taxation and Revenue Department

FOR YOUR INFORMATION

Tax Information/Policy Office ♦ P.O. Box 630 ♦ Santa Fe, New Mexico 87504-0630

INFORMATION ON RESEARCH AND DEVELOPMENT

This FYI focuses on the imposition of New Mexico gross receipts tax on the research and development industry.

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This information is as accurate as possible at time of publication. Subsequent legislation, new state regulations, and court cases may affect its accuracy. For the latest information please check the Taxation and Revenue Department's web site at www.tax.newmexico.gov.

DEFINITIONS

GROSS RECEIPTS

The New Mexico gross receipts tax is an excise tax imposed, as a percentage of gross receipts, on persons engaging in business in New Mexico for the privilege of engaging in business in New Mexico (Section 7-9-4 NMSA 1978).

The New Mexico Gross Receipts and Compensating Tax Act defines "gross receipts" as "the total amount of money or the value of other consideration received from selling property in New Mexico, from leasing or licensing property employed in New Mexico, from granting a right to use a franchise employed in New Mexico, from selling services performed outside New Mexico, the product of which is initially used in New Mexico, or from performing services in New Mexico." (Section 7-9-3.5 NMSA 1978).

INITIAL USE

The terms "initial use" and "initially used" means the first employment for the intended purpose. The following activities by the purchaser of the service do not constitute "initial use":

- 1) observation of tests conducted by the performer of the services;
- 2) participation in progress reviews, briefings, consultations and conferences conducted by the performer of the services;
- 3) review of preliminary drafts, drawings and other materials prepared by the performer of the services;
- 4) inspection of preliminary prototypes developed by the performer of the services; or
- 5) similar activities (Section 7-9-3(D) NMSA 1978).

RESEARCH AND DEVELOPMENT SERVICES

The term "research and development services" (R & D services) is defined as any activity engaged in for other persons for consideration, for one or more of the following purposes:

- 1) advancing basic knowledge in a recognized field of natural science;
- 2) advancing technology in a field of technical endeavor;
- 3) the development of a new or improved product, process or system with new or improved function, performance, reliability or quality, whether or not the new or improved product, process or system is offered for sale, lease or other transfer;
- 4) the development of new uses or applications for an existing product, process or system, whether or not the new use or application is offered as the rationale for

purchase, lease or other transfer of the product, process or system;

5) analytical or survey activities incorporating technology review, application, trade-off study, modeling, simulation, conceptual design or similar activities, whether or not offered for sale, lease or other transfer; or

6) the design and development of prototypes or the integration of systems incorporating advances, developments or improvements included in Paragraphs 1) through 5) of this subsection (Section 7-9-3(K) NMSA 1978).

AFFILIATED CORPORATION

An "affiliated corporation" means a corporation that directly or indirectly, through one or more intermediaries, controls, is controlled by, or is under common control with, the subject corporation. "Control" means ownership of stock in a corporation which represents at least eighty percent of the total voting power of that corporation and has a stated or par value equal to at least eighty percent of the total stated or par value of the stock of that corporation (Section 7-9-13.1(C) NMSA 1978).

R & D SERVICES PERFORMED INSIDE NEW MEXICO

In general, research and development services performed inside New Mexico are subject to gross receipts tax. However, there are two deductions which may apply to in-state R & D services and one deduction which may apply to the sale of tangible personal property in relation to an R & D contract. Deductions from gross receipts tax, like exemptions, are nontaxable amounts, but, unlike exemptions, deductions must be reported on the CRS-1 Form.

SALES TO OUT-OF-STATE BUYERS

Receipts from performing a **service** (including R & D services) inside New Mexico are deductible from gross receipts if: 1) the sale is made to an out-of-state buyer; 2) the buyer makes initial use of the product of the service outside New Mexico and 3) the buyer takes delivery of the product of the service outside New Mexico (Section 7-9-57 NMSA 1978). All three conditions must be met.

SALE OF A SERVICE FOR RESALE

Receipts from selling a **service** for resale may be deducted from gross receipts if the sale is made to a person who delivers a Type 5 Nontaxable Transaction Certificate (NTTC) to the seller. The subsequent sale must be in the ordinary course of business and subject to the gross receipts tax (Section 7-9-48 NMSA 1978). See examples 6 and 7 on pages 6 and 7.

SALE OF TANGIBLE PERSONAL PROPERTY TO A QUALIFIED FEDERAL CONTRACTOR OR SUBCONTRACTOR

Receipts from selling **tangible personal property** to a federal contractor or subcontractor may be deducted from the seller's gross receipts if the federal contractor or subcontractor executes a Type 15 NTTC to the seller. The federal contractor or subcontractor is authorized to issue a Type 15 NTTC only if the federal contract number is entered on the appropriate line of the Type 15 NTTC, all of the criteria contained in the agreement between New Mexico and the United States Government are met and the contracting agency is one of the United States agencies signatory to the agreement (see example 8 on page 7). Copies of the current agreements are available on our

web site at <http://www.tax.newmexico.gov/us-government-agreements-type-15-nttc.aspx>.

The criteria contained in the agreement between New Mexico and the United States Government are:

- 1) the contract must be for services;
- 2) the contract must be a cost or cost plus fixed fee;
- 3) the contract must contain a title-passing clause, whereby title to all tangible personal property purchased under the contract passes immediately to the federal government upon delivery to the contractor by the vendor; and
- 4) the services performed pursuant to the contract must be subject to the gross receipts tax.

A federal contractor or subcontractor may not issue a Type 15 NTTC for the purchase of services (Regulation 3.2.205.11 NMAC). Compensating tax will be due from the contractor if the contractor executes a Type 15 NTTC for the purchase of tangible personal property not specifically identified in the contract and not subsequently turned over to the United States Government.

R & D SERVICES PERFORMED OUTSIDE NEW MEXICO

Research and development services performed outside New Mexico the product of which is initially used in New Mexico are subject to the gross receipts tax (example 1 on page 5). All other services performed outside New Mexico are exempt from the gross receipts tax (Section 7-9-13.1 NMSA 1978).

The following R & D services are exempt from the gross receipts tax when performed outside New Mexico:

- 1) R & D services sold between affiliated corporations (example 2 on page 6);
- 2) R & D services sold to the United States **by** persons who are prime contractors operating facilities in New Mexico designated as national laboratories by act of Congress, other than 501(c)(3) organizations (example 3 on page 6); or
- 3) R & D services sold **to** persons who are prime contractors operating facilities in New Mexico designated as national laboratories by act of Congress, other than 501(c)(3) organizations (Section 7-9-13.1 NMSA 1978).

There are two national laboratories in New Mexico, neither of which is a 501(c)(3) organization:

- 1) Sandia National Laboratory (SNL)
- 2) Los Alamos National Laboratory (LANL)

Receipts from sales of services performed outside New Mexico to, or by, these laboratories are exempt.

GROSS RECEIPTS TAX NEXUS

A person performing research and development services outside New Mexico, when the product of the service is initially used in New Mexico, is subject to gross receipts tax if he has gross receipts tax nexus. Criteria sufficient to establish nexus in New Mexico include any of the following:

- 1) employing one or more New Mexico resident sales representatives;
- 2) employing one or more nonresident sales representatives who travel into New Mexico to solicit sales;
- 3) delivering goods into New Mexico in the business's own vehicles;
- 4) owning or leasing any type of property in New Mexico, including but not limited to, inventories, property stored or warehoused in New Mexico, real properties, property owned by the taxpayer and leased to customers, property leased to the taxpayer and vehicles or delivery trucks;
- 5) contracting with exclusive, non-employee sales agents who represent only the taxpayer's property;
- 6) having an authorized agent of the taxpayer in New Mexico who promotes sales;
- 7) having a service provider designated by the taxpayer to provide repair or other services for the taxpayer's customers in New Mexico;
- 8) leasing equipment used in New Mexico;
- 9) performing services in New Mexico;
- 10) maintaining a business location in New Mexico, or
- 11) selling a license used in New Mexico, including a license to access information or software provided through the Internet.

This listing is not an exclusive listing; other activities may establish nexus with New Mexico, depending on the facts. If it is not clear whether certain activities establish nexus with this state, it may be advisable to consult a tax attorney for assistance.

CREDIT FOR SALES TAX PAID TO ANOTHER STATE

R & D services performed outside New Mexico when the product of the service is initially used inside New Mexico may be subject to another state or political subdivision's gross receipts, sales or similar tax in addition to New Mexico's gross receipts tax. If the service provider has paid gross receipts, sales or a similar tax to the other state on those services, the service provider may take a credit of that amount, up to 5.125%, against any gross receipts tax due to New Mexico (Section 7-9-79.1 NMSA 1978). See example 9 on page 7.

GENERAL EXAMPLES

- 1) A Colorado architectural firm with a branch office in Las Cruces, New Mexico has been hired by a New Mexico client to design a building in Raton, New Mexico. The Colorado firm performs all the work in Colorado and upon completion of the architectural plans, sends them to its New Mexico client. Because the service is performed outside New Mexico but the product of the service is initially used (that is, first employed for its intended purpose) in New Mexico, the Colorado firm does have gross receipts in New Mexico. Its receipts, however, are exempt from gross receipts tax under Section 7-9-13.1(A) NMSA 1978 because architectural design of a building is not a research and development service.
- 2) X, a telecommunications conglomerate, has an affiliated corporation, Y, an out-of-state corporation with no presence in New Mexico, which performs R & D services for X. Y has developed an ultra-secure telephone system for X's facilities in New Mexico working on top-secret projects. Y sells the system to X. Y's receipts from X are exempt from gross receipts tax pursuant to Section 7-9-13.1(B)(1) NMSA 1978 which states that R & D services (*i.e.*, advancing technology in a field of technical endeavor) sold between affiliated corporations are exempt.
- 3) NASA contracts with Sandia National Laboratory in Albuquerque to perform simulated space tests, the results of which will be initially used at one of NASA's New Mexico facilities. Sandia performs the tests at its laboratory in California. Sandia's receipts from NASA, a U.S. governmental entity, are exempt from gross receipts tax under Section 7-9-13.1(B)(2) NMSA 1978 which states that receipts of a prime contractor operating facilities in New Mexico designated as national laboratories by act of Congress from performing R & D services, (*i.e.*, analytical activities incorporating simulation), outside New Mexico for the United States' initial use in New Mexico are exempt.
- 4) A California physics group is hired by White Sands Missile Range (WSMR) to pursue various avenues of fusion research. The California group has a business location in New Mexico but for this contract all the work will be performed in California. Scientists from the missile range will incorporate the results of the California group's research into research being performed at their location. Because the California group has a business location in New Mexico, they have nexus for gross receipts tax. Their receipts from performing R & D services (*i.e.*, advancing basic knowledge in a recognized field of natural science) outside New Mexico when the product of their service is being initially used in New Mexico are subject to gross receipts tax. The exemption provided by Section 7-9-13.1(B) NMSA 1978 does not include selling R & D services performed outside New Mexico the product of which is initially used in New Mexico when the sale is not to: 1) an affiliated corporation, 2) the U.S. government by a national laboratory or 3) a national laboratory.
- 5) An Idaho corporation contracts with the U.S. government to perform research and development work for use at a government installation in New Mexico. The Idaho company does not engage in any activity which would give it nexus with New Mexico. The Idaho company will perform all of the R & D work for the government contract in Idaho but will send reports and prototypes to New Mexico. Even though the Idaho corporation is performing R & D services outside New Mexico and the product of the service is initially used in New Mexico, their receipts are not subject to gross receipts tax because they do not have nexus for gross receipts tax in New Mexico.
- 6) A biological scientist consultant (A) in New Mexico agrees to perform research services for a biological research company (B) also located in New Mexico. B is under contract to a New Mexico pharmaceutical company (C). B submits A's research to C, separately stating A's charges plus a

10% markup. B reports and pays gross receipts tax on the amount it receives from C. B has met all the requirements set out for proper issuance of the Type 5 NTTC. A must report the receipts from B on the CRS-1 Form. However, A may deduct the entire amount if B executes a Type 5 NTTC to A.

7) Biological Research Company hires Janitorial Services to wash and disinfect laboratory equipment. Biological Research Company pays Janitorial Services and offers a Type 5 NTTC which Janitorial Services will not accept. Janitorial Services is correct in not accepting the NTTC. Janitorial Services' receipts from performing services for Biological Research are subject to the gross receipts tax. The washing and disinfecting services are not services purchased for resale; they are services consumed by Biological Research.

8) The United States government contracts with National Laboratory to carry out a sensitive defense-related research project. National Laboratory uses all-terrain vehicles in performing the research project. The contract between National Laboratory and the United States Government provides for reimbursement on a cost-plus basis for the vehicles, parts and other equipment necessary to carry out the project. National Laboratory purchases tires for the vehicles and executes a Type 15 NTTC to the tire store. The issuance of the certificate is proper. National Laboratory must enter its federal contract number on the certificate which it executes to the supplier. The tire store may deduct its receipts from this transaction.

9) A research and development company in the state of Washington has contracted with Kirtland Air Force Base in New Mexico to develop a new material for pilots' flying suits. The Washington-based R & D office also maintains a small office in Albuquerque staffed by three New Mexico resident employees to act as a communications link between the Washington company and its New Mexico clients. Initial use will be in New Mexico. The Washington company has nexus for gross receipts tax. Its receipts from performing this service are subject to New Mexico gross receipts tax because the exemption provided in Section 7-9-13.1 NMSA 1978 does not apply to receipts from performing a research and development service (*i.e.*, development of a new or improved product) outside New Mexico the product of which is initially used in New Mexico. But the state of Washington also imposes its business occupation tax on the Washington company's services. Pursuant to Section 7-9-79.1 NMSA 1978, the Washington company may consequently claim a credit in the amount of the business occupation tax paid to the state of Washington and apply the amount against its gross receipts tax liability in New Mexico.

TAXPAYER INFORMATION

The Department offers a variety of taxpayer information. Some information is free and other information must be purchased.

General Information. FYIs and Bulletins present general information with a minimum of technical language. All FYIs and Bulletins are free and available through all local tax offices, the Tax Information and Policy Office, and on the Internet. The Taxation and Revenue Department's Internet address is:

<http://www.tax.newmexico.gov>

Regulations. The Department establishes regulations to interpret and exemplify the various tax acts it administers. The Taxation and Revenue Department regulation book is available from the New Mexico Compilation Commission on a prepaid basis. The Compilation Commission also offers a compact disk of all statutes and regulations. The order form is available at all local tax offices, through the Tax Information and Policy Office and on the Department's web page at www.tax.newmexico.gov. Specific regulations are also available at the State Records Center or on its web page at www.nmcpr.state.nm.us/nmac.

Order regulation books directly from:

New Mexico Compilation Commission

<http://www.nmcompcomm.us/index.html>

Rulings. Rulings signed by the Secretary and approved by the Attorney General are written statements that apply to one or a small number of taxpayers. A taxpayer may request a ruling (at no charge) to clarify its tax liability or responsibility under specific circumstances. The request for a ruling must be in writing, include accurate taxpayer identification and the details about the taxpayer's situation, and be addressed to the Secretary of the Taxation and Revenue Department at P.O. Box 630, Santa Fe, NM 87504-0630. The taxpayer's representative, such as an accountant or attorney, may request a ruling on behalf of the taxpayer but must disclose the name of the taxpayer. While the Department is not required to issue a ruling when requested to do so, every request is carefully considered.

The Department will not issue a ruling to a taxpayer who is undergoing an audit, who has an outstanding assessment, or who is involved in a protest or litigation with the Department over the subject matter of the request. The Secretary may modify or withdraw any previously issued ruling and is required to withdraw or modify any ruling when subsequent legislation, regulations, final court decisions or other rulings invalidate a ruling or portions of a ruling. Taxation and Revenue Department rulings are compiled and available on the Department's web page free of charge at <http://www.tax.newmexico.gov/rulings.aspx>.

Public Decisions & Orders. All public decisions and orders issued by the hearing officers since July 1994 are compiled and available on the Department's web page free of charge at <http://www.tax.newmexico.gov/tax-decisions-orders.aspx>.

FOR FURTHER ASSISTANCE

The New Mexico Taxation and Revenue Department's local tax offices provide full service and information about Department-administered taxes, programs, and forms as well as specific information about your filing situation.

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This publication provides instructions or general information to the taxpayer. It does not constitute a regulation or ruling as defined under Section 7-1-60, *New Mexico Statutes Annotated, 1978*. Taxpayers and preparers are responsible for being aware of New Mexico tax laws and rules. Consult the Department directly if you have questions or concerns about information provided in this FYI.