Financial Advisory

Gaming & Hospitality

Public Policy Research

Real Estate Advisory

Regional & Urban Economics

NEVADA MARGIN TAX IMPACT ANALYSIS

August 2014

RCG ECONOMICS

3900 Paradise Road, Suite 209

Las Vegas, NV 89169

Main 702-967-3188

Fax 702-967-3196

www.rcg1.com

RCG ECONOMICS

Financial Advisory
Gaming & Hospitality
Public Policy Research
Real Estate Advisory
Regional & Urban Economics

August 6, 2014

Mr. Matt Griffin
Coalition to Defeat the Margin Tax Initiative
401 South Curry Street
Carson City, NV 89703

Re: Question 3 on November Ballot-Proposed Margin Tax Impact Analysis

Dear Mr. Griffin:

The Consultant Team of RCG Economics LLC ("RCG"), UNLV economist, Dr. Alan Schlottmann, and Eugenia Larmore, economist, are pleased to submit the referenced study to the Coalition to Defeat the Margin Tax Initiative.

This report is designed to provide useful information in assessing the potential impacts of the margin tax on Nevada's business community and provide a clearer understanding of this controversial proposed tax

Our report findings address three areas of potential impacts:

1. The total annual tax yield; taking into consideration of the effects and characteristics of business establishments that are part of affiliated groups;

2. As a component of the total tax yield, a detailed analysis and breakdown of the affiliated group impacts; and

3. A representative array of case studies, assessing the impacts on a specific set of businesses.

Also included in this report is link to margin tax calculator prepared by a Nevada CPA firm

If you have any questions, please do not hesitate to contact us at your convenience by phone at 702-967-3188 ext. 401 or by email at jrestrepo@rcg1.com.

Regards,

RCG Economics LLC

RCG Economics LLC

Attachment

3900 Paradise Road, Suite 209
Las Vegas, NV 89169
Main: 7202-967-3188
Fax: 702-967-3196
www.rcg1.com

TABLE OF CONTENTS

LIST OF TABLES

THE IMPACT OF THE PROPOSED MARGIN TAX ON NEVADA INDUSTRIES

EXECUTIVE SUMMARY

The Consultant Team of RCG Economics LLC ("RCG") and economists Dr. Alan Schlottmann and Eugenia Larmore were asked by the Coalition to Defeat the Margin Tax Initiative to identify the potential tax impact of the Question 3 on the November 2014 statewide ballot. The Margin Tax Initiative (called "The Education Initiative" by proponents) would impose a new state tax on all Nevada businesses with gross revenues in excess of $1 million (“M”) annually.

Major Findings

Our report findings address three areas of potential impacts:

1) The total annual tax yield, taking into consideration the effects and characteristics of business establishments that are part of affiliated groups and those not in affiliated groups;

2) As a component of the total tax yield, a detailed analysis and breakdown of the business entity impacts; and

3) A representative array of case studies, assessing the impacts on a specific set of businesses.

The bullet points below and the tables at the end of this Executive Summary summarize the key findings on the potential impacts of the proposed margin tax on Nevada’s industries. This study is based on a number of assumptions, which are outlined in the body of this report following the Executive Summary. Our analysis should be reviewed in its entirety to provide a full understanding of these findings. All data are for Fiscal Year (“FY”) 2013.

It is important to understand some of the terms used herein. The Initiative defines a “business entity” as “a corporation, partnership, proprietorship, limited-liability company, business association, joint stock company, holding company and any other person engaging in a business, and includes a combined group.” The Initiative also defines a “combined group” as “an affiliated group of business entities that is required to file a group return.”

The Initiative proposes to combine two or more business establishments sharing controlling ownership into “affiliated groups”, which is the term used in this report to represent these groups, instead of “combined groups”, since affiliated group is the more commonly used term. Individual businesses that do not share controlling interest with other businesses, and are stand-alone businesses are referred to as “establishments” herein in order to avoid confusion with the term “business entity”.

This analysis uses the term “business entity” when referring to a combination of affiliated groups and individual establishments, or when a differentiation between affiliated group and individual establishment does not need to be made.

The major findings of our analysis include:

- Annual Yield: The proposed margin tax would generate nearly **$800,000,000** in annual taxes on Nevada businesses.

- In FY-2013, there were **70,862** for-profit business **establishments** were analyzed herein.
    - Of the 70,862 establishments, **14,326** had common ownership with other establishments and were aggregated into **1,807** affiliated groups.
    - The remaining **56,536** establishments are individual businesses and do not have common ownership with another establishment.
    - The 1,807 affiliated groups were then combined with the 56,536 individual establishments in order to analyze the tax burdens on the resulting **58,343 business entities**.

- The proposed margin tax would affect **16,288 (27.9%)** of the 58,343 **business entities**.
    - Of the 1,807 **affiliated groups**, the proposed margin tax would affect **1,519 (84.1%)** groups comprised of **12,632** establishments; and
    - Of the 56,536 individual **establishments**, the proposed margin tax would affect **14,769 (26.1%)** of all establishments.

- **Business entities** affected by the proposed margin tax employ nearly **608,000** workers. This represents **63%** of all private establishment-based employees in the state in 2013. On a **per employee basis**, the margin tax would be an equivalent of **$1,314** per year.

- Based on Nevada’s 2013 population (2,700,551 from the Nevada Demographer’s Office), the margin tax would equate to **$288 per Nevada resident** annually.

- On a household (1,034,071) basis (Estimated based on Nevada Demographer 2010 and 2013 data), the margin tax would equate to **$722 per household** per year. This study does not address consumer costs. It would be difficult to predict how much of the $800M in new taxes imposed on Nevada businesses would be passed on to Nevada households via higher prices for goods and services, but it is a potentially large percentage.

- For all **business entities**, Nevada's top five industries with potentially the **highest annual margin tax** estimate include:
    1. **Retail Trade**: $109.3M margin tax/year.
    2. **Finance and Insurance**: $98.5M margin tax/year.
    3. **Health Care and Social Assistance**: $95.9M margin tax/year.
    4. **Wholesale Trade**: $90.6M margin tax/year.
    5. **Utilities**: $63.4M margin tax/year.

- For all business entities, the following are the top five industries that would be responsible for the highest shares of the proposed $800M margin tax:
    1. **Retail Trade**: 13.7% of total state margin tax amount/year.
    2. **Finance and Insurance**: 12.3% of total state margin tax amount/year.
    3. **Health Care and Social Assistance**: 12% of total state margin tax amount/year.
    4. **Wholesale Trade**: 11.4% of total state margin tax amount/year.
    5. **Utilities**: 7.9% of total state margin tax amount/year.

Case Studies

An important part of this analysis is the inclusion of a set of case studies that illustrate the margin tax liability for different types of companies. The 13 case studies used herein are based on actual information developed by the CPA firm of Fair, Anderson & Langerman (www.falcpa.com) for a set of its clients. The effective tax rate for each type of client is summarized below. Detailed calculations for each of these businesses are included in Appendix 1.

Industry	Effective Tax Rate	Combined Business Tax Rate; including Modified Business Tax
Commercial Insurance Broker	2.3%	3.1%
Design Studio	2.5%	2.8%
Residential Home Builder	3.7%	3.7%
Automotive & Accessories Retail Sales	5.3%	6.4%
Small Medical Practitioner	6.4%	10.1%
Patient Care Facility	6.5%	13.8%
Construction Subcontractor	7.6%	13.1%
Real Estate Broker, Version 1	11.4%	15.7%
Website Hosting and Services	17.1%	24.3%
Family Owned Rental Real Estate Investment Enterprise	18.3%	21.0%
Construction Wholesaler	31.6%	42.5%
Real Estate Broker, Version 2	82.1%	86.4%
Family Owned Restaurant	INFINITE	INFINITE

Summary of Estimated Proposed Margin Tax Impacts, State of Nevada

Nevada Industries Impacted by Margin Tax		% Affected by Margin Tax
Total Impacted Affiliated Groups	1,519	84.06%
Total Impacted Individual Establishments	14,769	26.12%
Total Impacted Business Entities	**16,288**	**27.92%**
Total Employment in Impacted Entities	607,696	63.10%
Estimated Modified Business Taxes, Impacted Entities	$245,951,077	
Annual Estimated Margin Tax Total	**$798,379,619**	
Annual Margin Tax per Affected Establishment Employee	$ 1,314	
Annual Margin Tax per Person (1)	$ 288	
Annual Margin Tax per Household (2)	$ 772	

(1) The Nevada Population (2,775,216) provided by the Nevada State Demographer's Office. The 2013 estimates were updated May 25, 2014.

(2) The number of Nevada households in 2013 (1,033,637) was computed by the Consultant using 2010 US Census data, including the ratio of household population to total population and the 2010 persons per household estimate of 2.65. The information was obtained from the Nevada Demographer's Office website.

Nevada's Most Impacted Industries by % of Total Statewide Margin Tax Amount

Industry	Estimated Margin Tax Amount	% of Total State Margin Tax Amount
Retail Trade	$109,319,925	13.7%
Finance and Insurance	$ 98,533,189	12.3%
Health Care and Social Assistance	$ 95,854,008	12.0%
Wholesale Trade	$ 90,640,820	11.4%
Utilities	$ 63,384,728	7.9%

I. INTRODUCTION

As noted in the Executive Summary, the RCG Economics team was retained by the Coalition to Defeat the Margin Tax to estimate the aggregate impact of the proposed Initiative on Nevada businesses. Below is a summary of the methodology used to estimate the overall tax revenue yield and the team's other major findings.

It is important to note that this study is <u>not</u> a company-level accounting analysis. That is, the impacts of the margin tax discussed herein are estimated by applying average Nevada industry data to business entity-level wages. All calculations, including estimated revenues, deductions, apportionment margin, taxable margin and MBT amounts are calculated at the business entity level.

As explained in the Executive Summary, it is critical to understand certain terms used in this report. The Initiative defines a "business entity" as "a corporation, partnership, proprietorship, limited-liability company, business association, joint stock company, holding company and any other person engaging in a business, and includes a combined group." The Initiative also defines a "combined group" as "an affiliated group of business entities that is required to file a group return."

The Initiative proposes to combine two or more business establishments sharing controlling ownership into "affiliated groups", which is the term used in this report to represent these groups, instead of the term "combined groups", since affiliated group is the more commonly used term. Individual businesses that do not share controlling interest with other businesses, and are stand-alone businesses are referred to as "establishments" in this analysis in order to avoid confusion with the term "business entity".

This analysis uses the term "business entity" when referring to a combination of affiliated groups and individual establishments, or when a differentiation between affiliated group and individual establishment does not need to be made.

This analysis has been conducted at the business entity-level, because the language of the Initiative states that the margin tax would apply to the cumulative revenues of a business entity (affiliated groups and establishments), rather than to individual companies.

As noted above, the Initiative defines an affiliated group as "a group of two of more businesses entities each of which is controlled by one or more common owners or by one or more of the members of the group". For example, one person may own a car wash business and a retail store with annual revenues of $450,000 and $600,000, respectively. Each company is considered an independent business establishment, but because they share a common owner, these companies would be combined into an affiliated group for the purposes of the Initiative.

This is an important component of the margin tax because, if treated as independent, neither establishment would qualify for the margin tax, as each has revenues of less than $1.0 million annually. However, the affiliated group has total revenues of $1.05 million; therefore, the entire amount would be taxed for margin tax purposes.

It is also important to note that this study is careful to omit “nonemployer establishments”, also known as nonemployer entities like sole proprietors, where owners are the sole employees of the establishment with no associated State payroll taxes.

The results herein are aggregated and reported at the 6-digit NAICS code level. Also, data are withheld for industries with less than five business entities per industry sector.

All other assumptions and details are discussed below.

METHODOLOGY AND ASSUMPTIONS

1. Salaries & Wages - This is the primary data on which our report is based. The Nevada Department of Employment, Training, and Rehabilitation’s (“DETR”) quarterly downloads of “covered employment” information have been combined to create a FY-2013[1] file of statewide establishments. Entities are then aggregated, based on their employment identification numbers (“EIN”) to develop “affiliated groups”. The resulting database provides the basis of employment and wage totals and a 6-digit NAICS code for each of the 58,343 non-tax exempt affiliated groups and individual establishments in the State.

This analysis includes all entities and affiliated groups that report employees and pay appropriate employee-related taxes to Nevada taxation agencies, since this is the source of DETR data. DETR does not report wage and employment data for nonemployer entities such as sole proprietors, where owners are the sole employees of the establishment with no associated State payroll taxes. The US Census Bureau, American FactFinder reports the number of establishment and receipts data for nonemployer establishments for the State of Nevada at the 2-digit NAICS code level. Table

[1] Fiscal year (FY) 2013 includes the period between July 1, 2012 and June 30, 2013.

1 summarizes these data and estimates the resulting receipts per establishment.

Table 1 at the end of this report shows that no Nevada industry has average nonemployer receipts per establishment of over $100,000. Similarly, according to the data from the IRS 2011 “Nonfarm Sole Proprietorship Returns: Selected Income Statement Items” report (latest), average business receipts per tax return for nonfarm sole proprietor firms were $55,153 in 1999, falling to $54,038 in 2011. Since the margin tax applies only to those entities with revenues of over $1million, this analysis does not include any nonemployer establishments in its calculation of margin tax impacts.

2. Estimated Total Business Entity Revenue (Total Revenue) - Revenue estimates are calculated using revenue data from the (latest) 2007 Economic Census for the State of Nevada, which is available for the majority of the State’s industries at the 2-digit NAICS level. For industries where revenue data are not reported by the 2007 Economic Census (Agriculture, Utilities and Unclassified), 2012 Nevada agricultural sales from USDA (Census of Agriculture) and 2011 US-level wages-to-revenue ratios from the Internal Revenue Service (Statistics of Income data) for the Utilities and Unclassified industries are estimated using the average wages-to-revenue ratio of all 2-digit industries. Table 2 at end of this report summarizes these data.

Revenue estimates for each business entity are inflated/deflated to FY-2013, based on 2008-2013 changes in total payroll as reported by DETR. They are then distributed to each business entity, based on their FY-2013 wages as a percent of total 2-digit industry wages.

Section 24 of the Initiative Petition, Total Revenue, to which the margin tax is applied, includes the following components:

Total Revenue = Business Receipts + Interest + Interest on Government Obligations + Rents + Royalties + Net Short-Term Capital Gain Less Net LT Loss + Net Long-Term Capital Gain Less Net ST Loss + Net Gain Noncapital Assets + Dividends from Domestic and Foreign Corporations + Other Receipts – (Bad Debts + Foreign Royalties + Foreign Dividends + Net Distributive Income + Net Loss Noncapital Assets + Dividends Received Deduction + Constructive Taxable Income from Related Foreign Corporations).

According to data definitions provided by the 2007 Economic Census report for each Nevada industry, revenue data for some industries includes the majority of the components above, while for other industries it includes only a few of the components (such as business receipts only). As a result, revenue estimated for each business entity may be conservatively underestimated, depending on the group's operating industry.

3. Gross Gaming Revenue Deduction - Section 24 of the Initiative Petition allows companies paying taxes under NRS 463.370 (state gaming license) to exclude the gross gaming revenue associated with this license from their Total Revenue estimate. NRS 463.370 applies to all nonrestricted licenses, which this analysis estimates to include NAICS codes 713210 and 721120. Total FY-2013 gross gaming revenue for all statewide nonrestricted entities of $10.9 billion[2] is distributed among all entities within these NAICS codes, based on their FY-2013 wages (as reported by DETR), as a percent of total wages for these two NAICS codes. This is deducted from Total Revenue as described in the Initiative petition.

4. Eligible Revenue - Per Section 22 of the Initiative Petition, only business entities with revenues of more than $1 million are eligible under the margin tax. Accordingly, the analysis herein excludes all entities/affiliated groups with revenues of less than $1 million.

5. Estimated Margin - This amount is the difference between Eligible Revenue (calculated in #4 above) and the allowable deduction for Cost of Goods Sold ("COGS") or Compensation as described in Section 23 of the Initiative Petition. COGS and Compensation deductions are estimated using IRS data for 2- and 3-digit NAICS codes and the ratios of these deductions to Total Revenue are created and applied to Eligible Revenue to estimate the Total Margin.

The COGS amount is a single line item reported to the IRS. This line item is used herein (see the discussion in the Limitations and Disclosures section of the report). The Compensation amount includes the Compensation of Officers, Salaries & Wages, Pension, Profit Sharing Plans, Stock, Annuity and Employee Benefit Programs line items as reported to the IRS.

According to Section 23 of the Initiative Petition, a business entity's margin cannot exceed 70%. If the COGS or the compensation deduction for a business entity is less than 30%, resulting in a margin of more than 70%, the standard 30% deduction is used.

6. Taxable Margin - The margin tax is applicable only to the portion of the business entity's margin generated within the State of Nevada. As a result, Section 28 of the petition discusses reducing the Estimated Margin by the ratio of its sales made within the state to its total sales ("apportionment margin"). This ratio was developed by the Consultant Team using the 2011 IMPLAN input-output model

[2] "June 2013 Nevada Gaming Revenues and Collections". Nevada Gaming Control Board.

for the State of Nevada. The model generates total out-of-state exports by industry sector, which are then subtracted from total output for each sector to arrive at the share of output that stays in-state for each industry sector. (See the Limitations and Disclosures section of this report for a discussion of IMPLAN model limitations.)

7. Margin Tax Amount - This amount is estimated by applying the 2% margin tax rate to the Taxable Margin (estimated in #6) for each business entity.

8. Modified Business Tax ("MBT") Credit - Per Section 22 of the Initiative Petition, businesses that make MBT payments under NRS 363A.130 and NRS 363B.110 can deduct these payments from their margin tax liability. The analysis estimates each business entity's MBT payments and subtracts these payments from the Margin Tax Amount described in #7 above.

The MBT amounts are calculated for every business entity, based on their FY-2013 quarterly wages, financial or non-financial institution status and health care benefits paid by the employer. Because DETR does not collect or report health care benefit payments, ratios of health care benefits versus gross wages calculated by the Nevada Department of Taxation are applied herein to each business entity, based on their 6-digit NAICS code.

The Initiative proposes temporary increases in MBT rates for financial institutions to pay for the implementation of the margin tax. The current 2% MBT rate for financial institutions is proposed to increase to 2.29% as of January 1, 2015, then to increase to 2.42% as of July 1, 2015, and then return to 2% as of July 1, 2016. The fluctuations in MBT rates for financial institutions are not incorporated into this analysis. The Appendix to this report reflects the existing 2% rate, since this is the on-going MBT rate for financial institutions beyond 2016. This is deducted from the Total Revenue as described in the Initiative Petition.

9. Net Margin Tax Amount - The estimated MBT credit (#8) is deducted from the Margin Tax Amount (#7) to arrive at the Net Margin Tax Amount to be paid by each business entity.

10. Industry Tax Impact Percentage - Due to confidentiality issues, this analysis cannot report any operating information on a business entity basis. As a result, the number of business entities, total employment, total revenue and ratio of estimated margin tax impact as a percent of total revenue are aggregated into a 6-digit NAICS code, which provides the impact of the margin tax on each industry without revealing sensitive business information.

11. Average Tax Impact per Entity - The estimated Net Margin Tax amount for each industry is divided by the number of business entities in the industry to arrive at the average margin tax amount per business entity within that industry.

II. Margin Tax Case Studies

As noted in the Executive Summary, a critical component of this analysis is the use of a set of 13 case studies illustrating what to potential the margin tax liability would be for different types of companies. The case studies used herein are based on actual information developed by the CPA firm of Fair, Anderson & Langerman (www.falcpa.com) for a set of its clients. The effective tax rate for each type of client is summarized below. Detailed calculations for each of these businesses are included in Appendix 1.

Industry	Effective Tax Rate	Combined Business Tax Rate;
Family Owned Restaurant	INFINITE	INFINITE
Real Estate Broker, V1	82.1%	86.4%
Construction Wholesaler	31.6%	42.5%
Family Owned Rental Real Estate Investment Enterprise	18.3%	21.0%
Website Hosting and Services	17.1%	24.3%
Real Estate Broker, V2	11.4%	15.7%
Construction Subcontractor	7.6%	13.1%
Patient Care Facility	6.5%	13.8%
Small Medical Practitioner	6.4%	10.1%
Automotive & Accessories Retail Sales	5.3%	6.4%
Residential Home Builder	3.7%	3.7%
Design Studio	2.5%	2.8%
Commercial Insurance Broker	2.3%	3.1%

III. Margin Tax Calculator

In addition to including a set of case studies in this report, we have also included a link to a margin tax calculator. The calculator can be found on the Nevada Manufacturers Association website at http://nvmanufacturers.org/hot-news/education-initiative/. The calculator, created by the CPA firm of Bullis and Company of Carson City (http://www.bullisandco.com/), can be used by companies to compute their margin tax liability.

Disclaimer: *The Consultant Team does not endorse this calculator. It is made available herein as a self-help tool for the independent use of third parties. The Consultant Team does not intend to provide tax advice. We cannot and do not guarantee the applicability or accuracy of the calculator regarding the individual tax circumstances of any specific business or industry. As such, the calculator is provided for illustrative purposes only. The Consultant Team advises any individual or business to seek personalized advice from a qualified professional regarding all tax accounting and finance issues.*

IV. Limitations, Assumptions and Disclosures

A number of limitations and data issues were faced in conducting this analysis. Some of these limitations are described below and must be considered when reviewing the results of the analysis.

- This analysis estimates the impact of the proposed margin tax on existing businesses and their performance in FY-2013. This is a "snapshot" analysis and does not estimate the impact of the proposed tax on business operations and consumer preferences, such as the reduction of purchases from consumers due to the increased cost of products or services. The proposed tax may affect purchasing behavior, leading to reduced sales tax revenue to the State, which could offset some margin tax revenues. These cost and price elasticity responses require a more detailed analysis and are not included in this report. Additionally, the analysis herein includes existing COGS data as a percent of sales, though it might be expected that businesses may attempt to reclassify their expenditures to increase their COGS deduction, reducing their margin tax impact.

- To comply with the language of the Initiative, business establishments are aggregated based on their employment identification numbers ("EIN") to create "affiliated groups". The Initiative states that establishments are considered to be part of an affiliated group if two or more establishments share controlling interest. Since public data regarding controlling interest is not readily available, this analysis uses the EIN methodology.

- This analysis may differ from other analyses estimating the impact of the proposed margin tax for the following reasons:

    a. Impacts of the proposed margin tax herein are estimated at the business entity level, as explained throughout. Estimating the margin tax liability for business establishments at the establishment-level may result in fewer businesses being subject to the tax, thereby underestimating the total impact of the margin tax.

    b. As discussed above, this analysis is a snapshot of current business behaviors in Nevada and does not account for any potential changes in behavior resulting from the margin tax. For example, if companies redefine their COGS expenditures to increase the COGS deduction, the margin tax amount estimated in this report may be overestimated.

- According to Initiative Petition, Section 83, *"If this act is not enacted and approved as provided in subsection 1, but is approved by the voters after the act has been referred or submitted to the voters pursuant to subsection 3 of Section 18 of Article 4 or subsection 3 of Section 2 of Article 19 of the Nevada Constitution… This section, sections 1 to 50, inclusive, sections 53 to 79, inclusive, and sections 81, 82 and 84 of this act become effective on 25 January 1, 2015."* As a result, this analysis assumes, if approved, that the margin tax would become effective January 1, 2015. However, it is unknown how revenues and other operating components would change between FY-2013 and 2015. In order to avoid additional assumptions, the analysis uses FY-2013 data with no adjustments to 2015.

- The Nevada Department of Taxation and regulatory bodies do not currently collect revenue information. As a result, revenue for each business entity is estimated herein, based on 2007 Economic Census revenue data for Nevada. Wage ratios (business entity wages as a ratio of total wages for its industry) reported by DETR are applied to the Economic Census revenues, by industry, to estimate each group's revenues. The resulting revenues are then inflated/deflated to FY-2013, based on 2008-2013 changes in total payroll by industry (DETR). The 2012 agriculture sales for Nevada (Census of Agriculture, USDA) and detailed US-level data provided by the IRS are used to estimate revenues for industries not reported by the Economic Census (agriculture and utilities).

- IRS tax returns data used to create wages-to-revenue ratios for the Utilities industry and all revenue adjustments (cost of goods sold-to-revenue, and compensation-to-revenue ratios) are not available at the state-level, but they are available at the national-level. IRS data are primarily used herein to develop business expense ratios to calculate deductions and to provide wage-revenue ratios for industries not reported by the 2007 Economic Census (Utilities). IRS data are reported for 6-digit, 3-digit and 2-digit NAICS codes. To avoid complications associated with recent changes in NAICS classifications and limited reporting due to disclosure issues, this analysis uses 2- and 3-digit NAICS code data.

- Apportionment margins for entities are estimated using the IMPLAN input-output model for Nevada. This analysis estimates the value of exports to total production for each industry sector, creating an apportionment ratio for the industries in the State. However, IMPLAN uses different codes from the NAICS industry codes utilized in the remainder of this report. IMPLAN codes do not perfectly translate to individual NAICS codes, reducing the accuracy of the apportionment margin estimated in this report.

- Section 25 of the Initiative Petition provides a detailed calculation of the COGS deduction that differs from the IRS definition. This analysis uses the IRS definition, since no detailed data are available from the IRS to calculate COGS using the Initiative Petition definition. The IRS reports COGS as a single line-item, so this amount cannot be adjusted to fit the

Initiative Petition's definition. The IRS is the only comprehensive source of this type of data known to the Consultant Team. As noted above, this study is not a company-level accounting analysis. In general, the IRS definition allows more COGS deductions than in the Initiative Petition. Thus, in the aggregate, assuming the same level of revenues and workforce wages and salaries, Nevada businesses would pay on a higher base-calculation under the Initiative definition than under the IRS definition used herein. Depending on the breadth and depth of this observation, the actual aggregate impact of the margin tax could therefore be higher than estimated herein.

- Section 26 of the Initiative Petition limits the amount of the compensation deduction to $300,000 per employee per year. As individual compensation at each establishment is unknown, this analysis does not have a basis to include any calculations associated with this limitation. Since this analysis estimates compensation amounts on a business entity basis, for groups with annual per employee compensation above $300,000 that opt to use the compensation deduction, the deduction may be overestimated herein, resulting in an underestimation of the actual margin tax impact.

- Affiliated groups can represent different industries. Affiliated groups are assigned an industry, based on their parent company's industry.

- As mentioned above, this analysis is partially based on average industry data and ratios. Due to a lack of company-specific financial data, this analysis does not account for characteristics that may be unique to an individual business entity or sub-industry, such as pass-through revenue or other relevant characteristics that may impact the calculation of the business entity's margin tax. For example, for an establishment with a large amount of pass-through revenue, the total revenue and the resulting taxable margin may be overestimated, resulting in an overestimation of the margin tax impact.

- Entities reported by DETR without industry definitions (assigned a NAICS code of "999999" or blanks) are assigned averages of all industry ratios before their tax impacts are calculated.

- Tax exempt industries and entities are <u>excluded</u> from the analysis, including NAICS codes: 611110 (elementary & secondary schools), 813 (religious, grantmaking, civic, professional, and similar organizations), 221310 (water supply & irrigation systems), 221320 (sewage treatment facilities), 92 (public administration), along with local, state and federal entities not classified as public administration, including all entities administered by the Nevada System of Higher Education.

V. MAJOR FINDINGS

The following are the major findings of our study on the impact of the proposed margin tax on Nevada industries. As noted above, this analysis is a "snapshot" of existing industry behaviors. It is expected that companies would change their behavior in response to the proposed tax. Some changes in behavior may include a redefinition of company COGS expenditures and changes in revenue and expenditure levels. Additionally:

- Appendix 2 summarizes the analysis findings for impacted industries at the 2-digit NAICS level, along with a summary of assumptions and methodology used in the analysis.

- With respect to total state tax revenues generated, this analysis estimates that the proposed margin tax would increase state taxes on businesses that provide goods and services in Nevada by approximately **$798.4 million** per year.

- The database on which this analysis is based includes **70,862 companies** (establishments) with approximately **963,000 employees**. The number of companies and employees does not match statewide totals due to the exclusion of tax-exempt entities.

These impacts are delineated in following table.

All Nevada Industries	
Total Establishments	72,969
Total Employment	1,111,984

Nevada Industries Not Exempt from Margin Tax	
Total Establishments	70,862
Total Employment	963,333

Source: Department of Employment, Training, and Rehabilitation and calculations by the Consultant Team.

- The resulting companies subject to the margin tax are aggregated into **1,807** affiliated groups and **56,536** individual establishments, based on their EINs.

- Of the **58,343** business entities, **16,288** are expected to be affected by the proposed margin tax. This is **27.9%** of all business entities included in the study[3].

Nevada Business Entities Affected by Margin Tax		% of Non-Tax Exempt
Total Affiliated Groups	1,519	84.06%
Total Individual Establishments	14,769	26.12%
Total Affected Business Entities	**16,288**	**27.92%**

[3] As discussed earlier, this analysis includes only companies that report employment data to the Nevada Department of Employment, Training, and Rehabilitation. This excludes sole proprietor-type businesses, which, as discussed above, are expected to be minimally impacted by the proposed margin tax due to their small size.

- An estimated **607,696** Nevadans are employed by the business entities expected to be affected by the proposed margin tax. This represents **63%** of all employees included in this study.

- For industries for which data can be released (those with 5 or more business entities), the annual estimated industry-wide net margin tax impact ranges from a low of **$2,213** for the Showcase, Partition, Shelving and Locker Manufacturing industry (NAICS 337215) to a high of **$48.3 million** for the Wholesale Trade Agents and Brokers industry (NAICS 425120).

- The top 25 industries with the highest estimated margin tax impact (in dollar terms) are summarized in Table 3 below.

- In addition to the Wholesale Trade Agents and Brokers, the other industries with the highest margin tax impact are Fossil Fuel Electric Power Generation (NAICS 221112), Commercial Banking (NAICS 522110), Supermarkets and Other Grocery (except Convenience) Stores (NAICS 445110), Offices of Physicians (except Mental Health Specialists) (NAICS 621111), General Medical and Surgical Hospitals (NAICS 622110), Professional Employer Organizations (NAICS 561330), Full-Time Restaurants, (NAICS 722511), Wired Telecommunications Carriers (NAICS 517110) and Offices of Lawyers (NAICS 541110).

- General Medical and Surgical Hospitals (NAICS 622110), Home Centers (NAICS 444110), Credit Card Issuing (NAICS 522210), Geothermal Electric Power Generation (NAICS 221116), Discount Department Stores (NAICS 452112), Professional Employer Organizations (NAICS 561330) and Electric Power Distribution (NAICS 221122).

VI. Closing Thoughts: The Long-Term

In contemplating the implementation of a possible new tax and revenue instrument, the first and most obvious question for Nevada is the level of revenues that such a tax would potentially yield. This report has addressed the potential revenue issue, while attempting to carefully balance the proposed language of the Initiative with the best available data to analyze its nuances and possible dollar impacts. Even so, by the nature of all such work, our estimate (or forecast) is based on the assumptions and limitations as outlined herein.

One critical question is the extent to which the proposed margin tax would be shared among consumers and employees. Businesses almost always pass along expenses to customers and/or adjust employees' wages and benefits wherever possible in a competitive market by increasing prices, reducing benefits, cutting hours, reducing wage increases, etc.

It is also important to recognize that the proposed new tax needs to be evaluated beyond the more obvious “yield” numbers. Often the proposed specific implementation of a new tax and its specific rules of exclusion and inclusion can create long-term business and economic issues beyond the conceptual nature of the tax itself. In addition, all new taxes involve some type of transfer among sectors (business, consumers, the public sector, etc.).

There are therefore a general series of questions that need to be considered in evaluating the impacts of the proposed margin tax on Nevada beyond the short-term yield of the tax:

Who would ultimately absorb most if not all of the margin tax liability - business or the consumer? How would this tax be shared among consumers, businesses, and employees?

How would the proposed margin tax and its specific implementation impact business growth and attraction to the Nevada over the long-term?

Would the margin tax be an additional source of revenue for education, or would it supplant existing dedicated revenues which would be shifted to other needs? What if the legislature simply rebalances its books and takes existing education funding away and uses the new margin tax revenues as a replacement?

Would the new revenues received by the public sector result in quality improvements for state programs? In the current case, the proposed margin tax is a targeted tax for education. It is reasonable to ask to what extent the new public revenues would impact areas of needed educational improvement in technology education, vocational education, and effectiveness of general education. How are these to be measured accurately, and what internal program allocations are assumed?

The purpose of our closing comments is to suggest three caveats for consideration. Before we present these three caveats, it is necessary to provide a frame of reference for the reader. It is also important to realize that there are a variety of opinions regarding what factors primarily drive a state’s economic growth, as well as the proper role of business synergies or industry clusters in that growth.

A Brief Frame of Reference

Studies of state growth comprise a significant area of interest in the current body of academic and business texts. Existing publications reflect two distinct schools of thought relevant to the investigation of Nevada's growth:

1. That which explores the regional growth process in terms of the general drivers of growth; and

2. That which attempts to suggest that public policy (such as detailed tax options and detailed infrastructure options) drives growth.

The first type of study tends to emphasize "traditional" locational determinants, such as regional market factors and transportation access, with a somewhat cursory treatment of policy implications, such as financial incentives, tax structure, and public infrastructure. In many respects, the traditional strand of economic literature has been successful in identifying the basic nature of the growth process.

In contrast, attempts to provide detailed public policy plans and outline proven and/or probable results tied to growth have at times been less successful. For example, a well-trained workforce is generally considered to be an important asset in economic development. However, the exact nature of the best possible government-driven development programs—and the associated funding mechanisms—for effectively creating or bolstering a highly skilled workforce are often debated because they can be more ambiguous and uncertain. It is this perplexing dichotomy between crucial growth factors that provides both the justification and point of departure for the three caveats below.[4]

Caveats

First, the aforementioned dichotomy becomes more crucial when it is recognized that a critical concept in regional economic analysis is the concept of "agglomeration". That is, businesses find a specific location good (or optimal) because of the presence of allied and/or supporting businesses and firms. This concept lies behind efforts by Nevada and other states to define specific industry clusters as critical to future growth and development. Although clustering synergies as explanations of market attraction have been included in regional economic analyses for decades, the recent inclusion of agglomeration into a focus on "clusters" in Nevada and other state-based business and economic studies and plans is striking.

Second, economic and financial literature is clear on the fact that Businesses generally invest in new ventures or expansions (building, plants, and equipment) through a combination of both internal financing (primarily generated from retained earnings

[4] These thoughts are similar to those previously expressed in 2003 by Schlottmann, who served as editor of a special issue on the perplexing issues of state economic growth; see Bartik, Boehm, Schlottmann (2003), "The Perplexing Literature on Growth and Change", The Review of Regional Studies Vol. 33, No. 1

and profits) and external financing (primarily debt financing from credit sources and investment funds). It is also generally recognized that such internal financing is influenced, as might be expected, by the business cycle and operating cost environment.

Because future investment by businesses leads to new job creation and economic growth, the potential impact of a proposed new tax on future investment activity needs to be considered. A new tax with new implementation requirements is simply not the same policy instrument as changing existing taxes, which are reasonably well understood by both Nevada businesses and consumers. Thus, the following questions must also be asked:

- What is the impact on business investment of a proposed new tax structure?
- How does a new tax structure compare to changing levels of current taxes already in place?
- How important are the proposed implementation and specific rules of a new tax as contrasted to the conceptual nature of the tax itself?

Third, Nevada public and private leaders have sought for many years to attract new firms to the state through their relocation, the expansion of new facilities, and incentives such as workforce training. Nevada has enhanced such activities in a variety of ways formally related to state functions and business groups that work closely with Nevada's economic development efforts. Organizations involved in these activities across the state include, for example, the Nevada workforce investment system and the Governor's Workforce Investment Board ("GWIB"), the Nevada Governor's Office of Economic Development ("GOED"), and the Las Vegas Global Economic Alliance ("LVGEA").

In contrast to modifications of the existing tax structure, reasonable questions occur with respect to a new tax and its potential impact on long-term business recruitment:

- What is the impact of a proposed new tax structure on business recruitment?
- How does a new tax structure compare to changing levels of current taxes already in place?
- Is it reasonable to either include or exclude certain new industries selected as critical to Nevada's future growth?
- Is the conceptual nature of the tax important for location decisions, or is it the rules of implementation along issues of inclusion and exclusion?

The Bottom Line

Unless the long-term impacts of the proposed margin tax to the Nevada economy and its residents are clearly understood, a full analysis of the economic and business ramifications of the tax on the state's economy is not possible. The proposed margin tax must be measured and evaluated on its impact to Nevada's economic growth potential, the state's economic development efforts, and last but not least, on future business investment. Anything short of this lays the groundwork for a potentially bad public policy that would negatively affect the state's economic future and the lives of it residents.

This report addresses only one aspect of these issues, namely the potential tax impact to Nevada businesses of the proposed margin tax, but the array of impacts is much broader and longer lasting.

Table 1: Establishments & Receipts Data for Nonemployer Establishments, Nevada

2007 NAICS Code	Meaning of 2007 NAICS Code	Number of Establishments	Receipts ($1,000)	Average Receipts/ Establishment
11	Agriculture, forestry, fishing and hunting	720	$ 27,950	$ 38,819
21	Mining, quarrying, and oil and gas extraction	436	35,938	82,427
22	Utilities	95	4,995	52,579
23	Construction	10,586	504,740	47,680
31-33	Manufacturing	2,178	130,210	59,784
42	Wholesale trade	3,345	307,359	91,886
44-45	Retail trade	15,264	695,502	45,565
48-49	Transportation and warehousing	6,040	372,037	61,596
51	Information	3,121	196,195	62,863
52	Finance and insurance	7,925	547,381	69,070
53	Real estate and rental and leasing	27,463	2,316,300	84,343
54	Professional, scientific, and technical services	27,377	1,465,129	53,517
56	Administrative and support and waste management and remediation services	15,571	425,807	27,346
61	Educational services	3,086	56,241	18,225
62	Health care and social assistance	13,110	503,111	38,376
71	Arts, entertainment, and recreation	13,826	616,149	44,565
72	Accommodation and food services	2,188	106,179	48,528
81	Other services (except public administration)	28,380	781,239	27,528
	Total for all sectors	**180,711**	**$9,092,462**	**$ 50,315**

Sources: US Census Bureau, American FactFinder. 2011 Non-employer Statistics: Geographic Area Series: Nonemployer Statistics for the US, States, Metropolitan Areas, and Counties: 2011. The data are for the State of Nevada.

Table 2: Estimated Total Revenue by Industry, Nevada

NAICS code	Meaning of 2007 NAICS Code	Employer value of sales, shipments, receipts, revenue, or business done ($1,000)	FY08 Annual Wages (DETR)	FY13 Annual Wages (DETR)	% Change	Estimated FY 2013 Total Revenue ($000)
11	Agriculture	NA	$ 67,831,395	$ 76,988,889	13.5%	$ 827,449
21	Mining, quarrying, and oil and gas extraction	5,743,123	924,342,438	1,310,648,391	41.8%	8,143,319
22	Utilities	NA	482,030,968	490,338,214	1.7%	10,292,702
23	Construction	29,314,420	6,797,546,786	2,732,487,798	-59.8%	11,783,853
31-33	Manufacturing	15,735,787	2,400,843,129	1,951,237,738	-18.7%	12,788,949
42	Wholesale trade	27,115,481	2,239,769,127	2,080,916,385	-7.1%	25,192,350
44-45	Retail trade	37,433,983	3,816,655,118	3,781,718,346	-0.9%	37,091,321
48-49	Transportation and warehousing	5,318,717	1,969,666,307	2,216,015,537	12.5%	5,983,937
51	Information1	3,524,137	812,431,968	777,561,654	-4.3%	3,372,878
52	Finance and insurance2	12,586,806	1,970,341,840	1,945,988,027	-1.2%	12,431,231
53	Real estate and rental and leasing	6,187,274	1,048,003,803	894,220,039	-14.7%	5,279,355
54	Professional, scientific, and technical services	8,991,000	3,481,831,794	3,307,497,986	-5.0%	8,540,825
55	Management of companies and enterprises	633,220	2,214,123,090	2,175,353,511	-1.8%	622,132
56	Administrative & support and waste management	8,407,671	2,325,168,585	2,287,703,256	-1.6%	8,272,199
61	Educational services	476,680	3,071,635,976	3,104,096,519	1.1%	481,717
62	Health care and social assistance	12,191,163	4,729,252,509	5,493,923,876	16.2%	14,162,348
71	Arts, entertainment, and recreation	3,367,067	882,718,373	831,765,536	-5.8%	3,172,711
72	Accommodation and food services	28,815,533	8,898,344,771	8,888,433,383	-0.1%	28,783,437
81	Other services (except public administration)	2,584,349	880,451,808	928,261,663	5.4%	2,724,683
99	Unclassified	NA	NA	NA	-	506,287
		$ 208,426,411	**$ 49,012,989,785**	**$ 45,275,156,748**	-7.6%	**$ 200,453,684**

Sources:

1. Receipts data from 2007 Economic Census, US Census Bureau. According to 2007 Economic Census Definitions, this analysis assumes "Employer value of Sales, etc." includes all business revenues, including dividends, rents, etc.

2. FY-2008 and FY-2013 Annual Payroll data from Department of Employment, Training and Rehabilitation.

3. Estimated FY-2013 Revenue for Agriculture using ratios of DETR FY-2013 wages, by entity, applied to 2013 agricultural sales in Nevada estimated from USDA Census of Agriculture 2007 & 2012 values.

4. Estimated FY-2013 Business Receipts for Utilities using DETR FY-2013 wages, by entity, and wages as percent of business receipts data from IRS 2011 Statistics of Income report, 2-digit NAICS code.

5. Estimated FY-2013 Business Receipts and Total Revenue for Unclassified sector using average ratios for all 2-digit NAICS codes provided in the IRS 2011 Statistics of Income report.

Table 3: Top 25 Industries, by Estimated Total Margin Tax Impact, Nevada

NAICS	Description	# of Business Entities	Actual FY2013 Employees	Estimated Net Tax Amount
425120	Wholesale Trade Agents and Brokers	1,374	5,237	$ 48,261,234
221112	Fossil Fuel Electric Power Generation	9	2,703	44,333,958
522110	Commercial Banking	35	9,713	35,099,354
445110	Supermarkets and Other Grocery (except Convenience) Stores	69	29,563	29,738,412
621111	Offices of Physicians (except Mental Health Specialists)	668	13,455	26,055,337
622110	General Medical and Surgical Hospitals	26	17,414	25,369,003
561330	Professional Employer Organizations	31	14,173	16,263,622
722511	Full-Service Restaurants	599	36,335	15,188,540
517110	Wired Telecommunications Carriers	38	3,716	13,868,827
541110	Offices of Lawyers	351	5,840	11,065,307
531210	Offices of Real Estate Agents and Brokers	116	3,508	10,547,813
561320	Temporary Help Services	150	16,501	10,457,411
541330	Engineering Services	140	5,655	10,285,030
621491	HMO Medical Centers	5	6,473	9,687,318
441110	New Car Dealers	80	6,668	8,760,641
443142	Electronics Stores	103	4,865	8,292,393
446110	Pharmacies and Drug Stores	58	4,526	7,849,868
523120	Securities Brokerage	25	700	7,173,946
442110	Furniture Stores	60	3,365	6,727,955
444110	Home Centers	7	4,860	6,626,671
531110	Lessors of Residential Buildings and Dwellings	133	3,731	6,616,893
522292	Real Estate Credit	70	1,243	6,474,234
531311	Residential Property Managers	100	3,433	6,307,704
722513	Limited-Service Restaurants	223	21,566	5,851,399
238212	Electrical Contractors and Other Wiring Installation Contractors	185	4,264	5,743,016

Source: DETR, Nevada Department of Taxation and Consultant Team.

APPENDIX 1: SAMPLE MARGIN TAX CASE STUDIES

Note: These examples do not constitute accounting, tax or legal advice and cannot be relied upon by any taxpayer for the purpose of avoiding penalties imposed under the Internal Revenue Code or any other taxing authority. These examples provide estimates only.

Proposed Margin Tax
Case Study Effective Tax Rates
2012 & 2013 Tax Return Info

Industry	Effective Tax Rate	Combined Business Tax Rate; including Modified Business Tax
Commercial Insurance Broker	2.3%	3.1%
Design Studio	2.5%	2.8%
Residential Home Builder	3.7%	3.7%
Automotive & Accessories Retail Sales	5.3%	6.4%
Small Medical Practitioner	6.4%	10.1%
Patient Care Facility	6.5%	13.8%
Construction Subcontractor	7.6%	13.1%
Real Estate Broker, Version 1	11.4%	15.7%
Website Hosting and Services	17.1%	24.3%
Family Owned Rental Real Estate Investment Enterprise	18.3%	21.0%
Construction Wholesaler	31.6%	42.5%
Real Estate Broker, Version 2	82.1%	86.4%
Family Owned Restaurant	INFINITE	INFINITE

*In the case of this particular restaurant business, the margin tax cannot be computed, because this business would be taxed even though it was generating a loss before applying the tax.

Source: Fair, Anderson & Langerman.

1. Commercial Insurance Broker
2013 Tax Return

Recap						
	Revenue as defined				**$**	**1,834,000**
	Operating Expenses				**$**	**(1,223,000)**
		Taxable Income			**$**	**611,000**
Alternative Margin Calculations						
A.	**70% of Revenues**				**$**	**1,283,800**
B.	**Cost of Goods Sold**					
	Revenue		**$**	**1,834,000**		
	Cost of Goods Sold		**$**	**-**	**$**	**1,834,000**
C.	**Compensation**					
	Revenues		**$**	**1,834,000**		
	Compensation		**$**	**(878,000)**	**$**	**956,000**
Smallest Taxable Margin					**$**	**956,000**
		Tax Rate				**2%**
		Tentative Tax			**$**	**19,120**
		MBT Offset			**$**	**(5,100)**
		Tax			**$**	**14,020**
		% to Taxable Income				**2.3%**

Note: This assumes a taxpayer friendly administration definition of "pass-through" revenue.

Source: Fair, Anderson & Langerman.

2. Design Studio
2012 Tax Return

Recap				
	Revenue as defined			**$ 1,001,780**
	Operating Expenses			**$ (729,780)**
		Taxable Income		**$ 272,000**
Alternative Margin Calculations				
A.	**70% of Revenues**			**$ 701,246**
B.	**Cost of Goods Sold**			
	Revenue		**$ 1,001,780**	
	Cost of Goods Sold		**$ -**	**$ 1,001,780**
C.	**Compensation**			
	Revenues		**$ 1,001,780**	
	Compensation		**$ (627,000)**	**$ 374,780**
Smallest Taxable Margin				**$ 374,780**
		Tax Rate		**2%**
		Tentative Tax		**$ 7,496**
		MBT Offset		**$ (650)**
		Tax		**$ 6,846**
		% to Taxable Income		**2.5%**

Note: This assumes a taxpayer friendly administration definition of "pass-through" revenue.

Source: Fair, Anderson & Langerman.

3. Residential Home Builder
2012 Tax Return

Recap				
Revenue as defined			$	13,330,000
Cost of Goods as defined			$	(8,830,000)
Operating Expenses			$	(2,099,000)
	Taxable Income		$	2,401,000
Alternative Margin Calculations				
A. 70% of Revenues			$	9,331,000
B. Cost of Goods Sold				
Revenue	$	13,330,000		
Cost of Goods Sold	$	(8,830,000)	$	4,500,000
C. Compensation				
Revenues	$	13,330,000		
Compensation	$	519,000	$	13,849,000
Smallest Taxable Margin			$	4,500,000
	Tax Rate			2%
	Tentative Tax		$	90,000
	MBT Offset		$	(1,665)
	Tax		$	88,335
	% to Taxable Income			3.7%

Note: This assumes a taxpayer friendly administration definition of "pass-through" revenue.

Source: Fair, Anderson & Langerman.

4. Automotive & Accessories Retail Sales
2012 Tax Return

Recap				
Revenue as defined			**$**	**31,137,000**
Cost of Goods as defined			**$**	**(19,622,000)**
Operating Expenses			**$**	**(7,929,000)**
	Taxable Income		**$**	**3,586,000**
Alternative Margin Calculations				
A. 70% of Revenues			**$**	**21,795,900**
B. Cost of Goods Sold				
Revenue	**$**	**31,137,000**		
Cost of Goods Sold	**$**	**(19,622,000)**	**$**	**11,515,000**
C. Compensation				
Revenues	**$**	**31,137,000**		
Compensation	**$**	**(4,307,000)**	**$**	**26,830,000**
Smallest Taxable Margin			**$**	**11,515,000**
	Tax Rate			**2%**
	Tentative Tax		**$**	**230,300**
	MBT Offset		**$**	**(40,298)**
	Tax		**$**	**190,002**
	% to Taxable Income			**5.3%**

Note: This assumes a taxpayer friendly administration definition of "pass-through" revenue.

Source: Fair, Anderson & Langerman.

5. Small Medical Practitioner
2013 Tax Return

Recap				
	Revenue as defined			**$ 3,790,000**
	Operating Expenses			**$ (3,360,000)**
		Taxable Income		**$ 430,000**
Alternative Margin Calculations				
A.	**70% of Revenues**			**$ 2,653,000**
B.	**Cost of Goods Sold**			
	Revenue		**$ 3,790,000**	
	Cost of Goods Sold		**$ -**	**$ 3,790,000**
C.	**Compensation**			
	Revenues		**$ 3,790,000**	
	Compensation		**$ (1,624,000)**	**$ 2,166,000**
Smallest Taxable Margin				**$ 2,166,000**
		Tax Rate		**2%**
		Tentative Tax		**$ 43,320**
		MBT Offset		**$ (16,000)**
		Tax		**$ 27,320**
		% to Taxable Income		**6.4%**

Note: This assumes a taxpayer friendly administration definition of "pass-through" revenue.

Source: Fair, Anderson & Langerman.

6. Patient Care Facility
2012 Tax Return

Recap					
	Revenue as defined			**$**	**11,232,000**
	Operating Expenses			**$**	**(10,416,000)**
		Taxable Income		**$**	**816,000**
Alternative Margin Calculations					
A.	**70% of Revenues**			**$**	**7,862,400**
B.	**Cost of Goods Sold**				
	Revenue	**$**	**11,232,000**		
	Cost of Goods Sold	**$**	**-**	**$**	**11,232,000**
C.	**Compensation**				
	Revenues	**$**	**11,232,000**		
	Compensation	**$**	**(5,590,000)**	**$**	**5,642,000**
Smallest Taxable Margin				**$**	**5,642,000**
		Tax Rate			**2%**
		Tentative Tax		**$**	**112,840**
		MBT Offset		**$**	**(60,000)**
		Tax		**$**	**52,840**
		% to Taxable Income			**6.5%**

Note: This assumes a taxpayer friendly administration definition of "pass-through" revenue.

Source: Fair, Anderson & Langerman

7. Construction Subcontractor
2013 Tax Return

Recap					
	Revenue as defined			**$**	**1,476,000**
	Cost of Goods as defined			**$**	**(970,000)**
	Operating Expenses			**$**	**(429,000)**
		Taxable Income		**$**	**77,000**
Alternative Margin Calculations					
A.	**70% of Revenues**			**$**	**1,033,200**
B.	**Cost of Goods Sold**				
	Revenue	**$**	**1,476,000**		
	Cost of Goods Sold	**$**	**(970,000)**	**$**	**506,000**
C.	**Compensation**				
	Revenues	**$**	**1,476,000**		
	Compensation	**$**	**(831,000)**	**$**	**645,000**
Smallest Taxable Margin				**$**	**506,000**
		Tax Rate			**2%**
		Tentative Tax		**$**	**10,120**
		MBT Offset		**$**	**(4,300)**
		Tax		**$**	**5,820**
		% to Taxable Income			**7.6%**

Note: This assumes a taxpayer friendly administration definition of "pass-through" revenue.

Source: Fair, Anderson & Langerman.

8. Real Estate Broker, Version 1
2012 Tax Return

Recap				
	Revenue as defined			**$ 15,186,000**
	Operating Expenses			**$ (13,956,000)**
		Taxable Income		**$ 1,230,000**
Alternative Margin Calculations				
A.	**70% of Revenues**			**$ 10,630,200**
B.	**Cost of Goods Sold**			
	Revenue		**$ 15,186,000**	
	Cost of Goods Sold		**$ -**	**$ 15,186,000**
C.	**Compensation**			
	Revenues		**$ 15,186,000**	
	Compensation		**$ (5,526,000)**	**$ 9,660,000**
Smallest Taxable Margin				**$ 9,660,000**
		Tax Rate		**2%**
		Tentative Tax		**$ 193,200**
		MBT Offset		**$ (53,298)**
		Tax		**$ 139,902**
		% to Taxable Income		**11.4%**

Note: This assumes a taxpayer friendly administration definition of "pass-through" revenue.

Source: Fair, Anderson & Langerman.

9. Web Hosting and Services
2012 Tax Return

Recap					
	Revenue as defined			$	5,620,000
	Operating Expenses			$	(5,336,000)
		Taxable Income		$	284,000
Alternative Margin Calculations					
A.	**70% of Revenues**			$	3,934,000
B.	**Cost of Goods Sold**				
	Revenue	$	5,620,000		
	Cost of Goods Sold	$	-	$	5,620,000
C.	**Compensation**				
	Revenues	$	5,620,000		
	Compensation	$	(2,166,000)	$	3,454,000
Smallest Taxable Margin				$	3,454,000
		Tax Rate			2%
		Tentative Tax		$	69,080
		MBT Offset		$	(20,400)
		Tax		$	48,680
		% to Taxable Income			17.1%

Note: This assumes a taxpayer friendly administration definition of "pass-through" revenue.

Source: Fair, Anderson & Langerman.

10. Family Owned Rental Real Estate Investment Enterprise
2012 Tax Return

Recap					
	Revenue as defined			$	6,709,000
	Excludable K-1 Income			$	697,000
	Operating Expenses			$	(6,959,000)
		Taxable Income		$	447,000
Alternative Margin Calculations					
A.	**70% of Revenues**			$	4,696,300
B.	**Cost of Goods Sold**				
	Revenue	$	6,709,000		
	Cost of Goods Sold	$	-	$	6,709,000
C.	**Compensation**				
	Revenues	$	6,709,000		
	Compensation	$	(1,592,000)	$	5,117,000
Smallest Taxable Margin				$	4,696,300
		Tax Rate			2%
		Tentative Tax		$	93,926
		MBT Offset		$	(12,016)
		Tax		$	81,910
		% to Taxable Income			18.3%

Note: Example based on TX Franchise Tax calculation which taxes gross rents notwithstanding contradictory language. The Nevada Act contains the same language.

Source: Fair, Anderson & Langerman.

11. Construction Wholesaler
2012 Tax Return

Recap					
	Revenue as defined			**$**	**4,819,000**
	Cost of Goods as defined			**$**	**(3,121,000)**
	Operating Expenses			**$**	**(1,618,000)**
		Taxable Income		**$**	**80,000**
Alternative Margin Calculations					
A.	**70% of Revenues**			**$**	**3,373,300**
B.	**Cost of Goods Sold**				
	Revenue	**$**	**4,819,000**		
	Cost of Goods Sold	**$**	**(3,121,000)**	**$**	**1,698,000**
C.	**Compensation**				
	Revenues	**$**	**4,819,000**		
	Compensation	**$**	**(1,007,000)**	**$**	**3,812,000**
Smallest Taxable Margin				**$**	**1,698,000**
		Tax Rate			**2%**
		Tentative Tax		**$**	**33,960**
		MBT Offset		**$**	**(8,700)**
		Tax		**$**	**25,260**
		% to Taxable Income			**31.6%**

Note: This assumes a taxpayer friendly administration definition of "pass-through" revenue.

Source: Fair, Anderson & Langerman.

12. Real Estate Broker, Version 2
2012 Tax Return

Recap				
Revenue as defined			$	75,894,000
Commissions			$	(60,708,000)
Operating Expenses			$	(13,956,000)
	Taxable Income		$	1,230,000
Alternative Margin Calculations				
A. 70% of Revenues			$	53,125,800
B. Cost of Goods Sold				
Revenue	$	75,894,000		
Cost of Goods Sold	$	-	$	75,894,000
C. Compensation				
Revenues	$	75,894,000		
Compensation	$	(5,526,000)	$	70,368,000
Smallest Taxable Margin			$	53,125,800
	Tax Rate			2%
	Tentative Tax		$	1,062,516
	MBT Offset		$	(53,298)
	Tax		$	1,009,218
	% to Taxable Income			82.1%

Note: To avoid this result, a taxpayer friendly definition of "pass-through revenue" is required.

Source: Fair, Anderson & Langerman.

13. Family Owned Restaurant
2012 Tax Return

Recap						
	Revenue as defined				**$**	**1,833,000**
	Cost of Goods as defined				**$**	**(1,008,000)**
	Operating Expenses				**$**	**(1,270,000)**
		Taxable Income			**$**	**(445,000)**
Alternative Margin Calculations						
A.	**70% of Revenues**				**$**	**1,283,100**
B.	**Cost of Goods Sold**					
	Revenue		**$**	**1,833,000**		
	Cost of Goods Sold		**$**	**(1,008,000)**	**$**	**825,000**
C.	**Compensation**					
	Revenues		**$**	**1,833,000**		
	Compensation		**$**	**(724,000)**	**$**	**1,109,000**
Smallest Taxable Margin					**$**	**825,000**
		Tax Rate				**2%**
		Tentative Tax			**$**	**16,500**
		MBT Offset			**$**	**(3,387)**
		Tax			**$**	**13,113**
		% to Taxable Income				**INFINITE**

Note: This assumes a taxpayer friendly administration definition of "pass-through" revenue.

Source: Fair, Anderson & Langerman.

APPENDIX 2: ESTIMATED ANNUAL MARGIN TAX - AFFECTED INDUSTRIES & BUSINESS ENTITIES, 2-DIGIT NAICS CODE

NAICS	Description	# of Group	Actual FY2013 Employees	Estimated Total Revenue	Estimated Net Total Eligible Revenue	Estimated Margin	Estimated Taxable Margin	Estimated Gross Tax Amount	Estimated MBT Credit	Estimated Net Tax Amount
11	Agriculture, Forestry, Fishing and Hunting	152	2,147	$ 716,149,745	$ 716,149,745	$ 375,104,578	$ 158,298,860	$ 3,165,977	$ 372,747	$ 2,793,230
21	Mining, Quarrying, and Oil and Gas Extraction	134	3,801	1,599,671,912	1,599,671,912	819,867,687	321,027,549	6,420,551	2,580,753	3,839,798
22	Utilities	31	4,444	10,291,667,037	10,291,667,037	4,361,000,774	3,399,458,734	67,989,175	4,604,447	63,384,728
23	Construction	1,871	46,865	10,835,994,855	10,835,994,855	3,048,893,864	3,019,189,761	60,383,795	20,818,082	39,565,713
31	Manufacturing	87	3,600	829,438,906	829,438,906	246,939,511	132,905,999	2,658,120	1,144,696	1,513,424
32	Manufacturing	224	6,148	1,783,773,366	1,783,773,366	598,270,019	234,111,453	4,682,229	2,303,322	2,378,907
33	Manufacturing	278	3,655	1,035,574,373	1,035,574,373	424,907,515	101,159,015	2,023,180	932,287	1,090,894
42	Wholesale Trade	2,674	30,954	24,523,144,720	24,523,144,720	6,859,179,727	5,315,212,667	106,304,253	15,663,434	90,640,820
44	Retail Trade	1,751	98,466	27,968,776,002	27,968,776,002	7,983,940,404	6,848,077,909	136,961,558	27,641,633	109,319,925
45	Retail Trade	578	31,129	8,261,276,957	8,261,276,957	2,703,643,618	1,989,481,088	39,789,622	8,091,415	31,698,206
48	Transportation and Warehousing	328	23,272	3,286,788,184	3,286,788,184	2,270,328,864	1,037,414,147	20,748,283	11,001,088	9,747,195
49	Transportation and Warehousing	130	15,190	1,776,712,040	1,776,712,040	1,050,948,454	644,009,367	12,880,187	6,245,545	6,634,642
51	Information	321	11,723	3,186,556,263	3,186,556,263	2,222,840,388	1,900,255,501	38,005,110	6,359,174	31,645,936
52	Finance and Insurance	932	27,795	11,869,337,260	11,869,337,260	7,491,855,608	6,211,585,986	124,231,720	25,698,530	98,533,189
53	Real Estate and Rental and Leasing	688	18,479	4,628,107,081	4,628,107,081	3,239,674,957	2,323,376,216	46,467,524	6,831,399	39,636,125
54	Professional, Scientific, and Technical Services	1,386	34,784	6,840,629,661	6,840,629,661	4,546,943,483	4,096,866,360	81,937,327	23,359,071	58,578,257
56	Administrative and Support and Waste Management and Remediation Services	1,006	67,775	7,077,106,315	7,077,106,315	4,032,766,952	3,391,976,995	67,839,540	19,384,614	48,454,926
61	Educational Services	86	3,747	370,452,837	370,452,837	229,488,872	225,631,507	4,512,630	1,686,544	2,826,087
62	Health Care and Social Assistance	1,661	77,672	12,821,295,603	12,821,295,603	6,816,345,359	6,808,927,132	136,178,543	40,324,535	95,854,008
71	Arts, Entertainment, and Recreation	272	12,079	1,776,589,932	1,770,671,364	1,188,569,437	871,612,502	17,432,250	4,053,771	13,378,479
72	Accommodation and Food Services	1,013	69,849	5,555,604,529	5,555,604,529	3,294,723,679	1,993,825,322	39,876,506	13,525,439	26,351,068
81	Other Services (except Public Administration)	546	13,756	2,046,124,293	2,046,124,293	1,219,111,011	1,034,320,278	20,686,406	3,215,305	17,471,101
99	Unclassified	139	366	336,914,387	336,914,387	197,477,837	157,810,451	3,156,209	113,247	3,042,962
	TOTAL	16,288	607,696	$ 149,417,686,258	$ 149,411,767,690	$ 65,222,822,599	$ 52,216,534,797	$ 1,044,330,696	$ 245,951,077	$ 798,379,619

Source: DETR, Nevada Department of Taxation and Consultant Team.

APPENDIX 3: ABOUT THE TEAM

JOHN RESTREPO, PRINCIPAL – RCG ECONOMICS LLC (WWW.RCG1.COM)

John Restrepo is the Principal of RCG Economics LLC (RCG). RCG is based in Las Vegas, Nevada, and was founded in 1997. It is the oldest and most established regional economics, real estate consulting and public policy research firm in Nevada. John has been providing regional economic and real estate consulting services for more than 35 years, 26 of those years in Nevada from the firm's office in Las Vegas.

Prior to starting RCG, he was the Director of Financial Advisory Services in the Las Vegas office of Coopers & Lybrand (now PricewaterhouseCoopers). John received his B.A. in Economics from the University of Louisiana and his M.A. and in Latin American Studies/Economics from Louisiana State University.

As an economist and advisor to state and local governments, educational organizations and the private sector, John has prepared numerous macroeconomic forecasts, demographic projections, real estate market research analyses, lodging/hospitality feasibility studies, tax revenue estimates, as well as a variety of economic impact and fiscal impact reports.

His clients include a broad range of the most prominent private and public organizations concerned with the interplay of regional economic trends, urban development and public policy issues, combined with the related questions of economic growth, diversification and development.

John was:

- The 2008 President of the Southern Nevada chapter of NAIOP, the Commercial Real Estate Association
- Appointed by Governor Kenny Guinn in 1990 to chair the Governor's "Task Force on Long-Term Financial Analysis & Planning"
- Chairman of the Nevada Economic Forum, 2008-2011. The Economic Forum produces two-year revenue forecasts for state's general fund

Currently, he is:

- Chairman of the Nevada Mining Oversight and Accountability Commission, appointed by Governor Brian Sandoval in 2011
- A board member of NAIOP-Southern Nevada
- Member of the Metro Las Vegas Chamber Government Affairs Committee
- Member of the Vegas PBS Board of Directors
- Chairman of the Advisory Committee to the UNLV Department of EconomicsMember of the Western Blue Chip Economic panel of ASU

Through RCG, John also jointly publishes Southern Nevada's leading monthly economic and investment newsletter, ***The Stat Pack***, with Hightower Advisors of Las Vegas. He also recently launched ***Nevada by the Numbers***, a public policy blog.

ALAN SCHLOTTMANN, PHD - PROFESSOR OF ECONOMICS, UNLV

Alan has been on the faculty of UNLV since 2001. He is former William Stokely Scholar in the Stokely Management Center at the University of Tennessee. He serves on the Governors Workforce Investment Board for the State of Nevada on the Logistics and Service Sector Council with a crossover to manufacturing. Alan is a graduate of Washington University in St Louis where he received his B.A., M.A. and Ph.D.

As both an academic and a business owner, Alan has received commendations from the City of Las Vegas and the State of Nevada for his advisory roles on business development and workforce training initiatives. Alan has extensive real-world experience in economic development and firm location decisions, particularly with respect to the location of the automotive sector in the Southeast United States.

For 20 years, he was the associate editor of the *Journal of Regional Science*. He is also the former editor of the *Review of Regional Studies*. His publications have focused on regional economic development and related state tax and infrastructure issues. He has worked with local governments in Southern Nevada, including the Cities of Henderson, Las Vegas and North Las Vegas and Clark County. His investigative studies include work for the investigative arm of Congress, the U.S. GAO (General Accounting Office).

EUGENIA LARMORE - EKAY ECONOMIC CONSULTANTS, INC. (WWW.EKAYCONSULTANTS.COM)

Eugenia graduated from the University of Nevada, Reno with a MBA and a B.S. degree in International Business and Marketing with a minor in Economics. She is currently pursuing a Ph.D. in Economics from the University of Nevada, Reno. Eugenia's areas of practice include economic damages, financial analysis, fiscal and economic impact analyses, feasibility, public policy, tax, and other economic analyses. Eugenia has considerable experience in local government finance, specifically as it relates to fiscal and economic impact and policy impact analyses. In addition, she has worked nationally with various gaming operators and local governments in gaming feasibility, fiscal and economic impacts of gaming and gaming litigation cases.

Eugenia is a nationally certified valuation analyst (CVA), certified in management accounting (CMA) and master analyst in financial forensics (MAFF), specializing in Financial Litigation.

She is a member of the following professional organizations:

- National Association of Certified Valuation Analysts
- Commercial Real Estate Development Association
- Institute of Management Accountants
- National Association of Forensic Economics

Endnotes:

1. This analysis includes data only for companies impacted by the proposed Margin Tax (those with Total Revenue of over $1 million and those where the estimated Gross Margin Tax Impact exceeds estimated MBT credits).

2. Companies are aggregated into "affiliated groups", based on their Employee Identification Number (“EIN”) as reported to Nevada Department of Employment, Training and Rehabilitation (“DETR”).

3. It is important to understand some terms used throughout the report. The Initiative defines a “business entity” as “a corporation, partnership, proprietorship, limited-liability company, business association, joint stock company, holding company and any other person engaging in a business, and includes a combined group.” The Initiative also defines a “combined group” as an affiliated group of business entities that is required to file a group return.”

4. The Initiative proposes to combine two or more business establishments sharing controlling ownership into “affiliated groups”, which is the term used in this report to represent these groups, instead of combined groups, as affiliated group is the more commonly used term. Individual businesses that do not share controlling interest with other businesses, and are stand-alone businesses are referred to as “establishments” herein to avoid confusion with the term “business entity”. This analysis uses the term “business entity” when referring to a combination of affiliated groups and individual establishments, or when a differentiation between affiliated group and individual establishment does not need to be made.

5. Actual employee data per business entity are collected from DETR for fiscal year (FY) 2013, which includes the period July 1, 2012 through June 30, 2013.

6. Total Revenue business entity is estimated as follows:
   a) Revenue by 2-digit NAICS code is provided through the 2007 U.S. Census Bureau for the majority of industries. This revenue is inflated to FY-2013 levels by using the percent change in Nevada employee wages for each 2-digit industry between FY-2008 and FY-2013 as reported by DETR.

      - FY-2013 revenue for the Agriculture industry is estimated using ratios of DETR FY-2013 wages, by entity, applied to 2013 agricultural sales in Nevada estimated from USDA Census of Agriculture 2007 and 2012 values.

      - FY-2013 revenue for Utilities is estimated using DETR FY-2013 wages, by entity, and wages as a percent of revenue data from IRS 2011 Statistics of Income report, 2-digit NAICS code.

      - FY 2013 revenue for Unclassified industries is estimated using average revenue to wages ratios for all 2-digit NAICS codes provided in the IRS 2011 Statistics of Income report.

   b) Revenue is distributed among all business entities by the percent of each group's FY-2013 wages of the total 2-digit NAICS industry's wages.

7. Gaming Revenue Deduction is estimated using statewide FY-2013 gross gaming revenue for all gaming entities of $10.9 billion, distributed among business entities, based on the percent of each group's FY-2013 wages of the total wages for all gaming entities. Gaming

revenue from "June 2013 Nevada Gaming Revenues and Collections". Nevada Gaming Control Board.

8. Estimated Net Total Revenue = Estimated Total Revenue - Actual Gaming Revenue Reduction.

9. Estimated Eligible Revenue includes only revenue for those business entities with estimated Net Total Revenue of over $1 million.

10. Deductions are estimated as follows:
    a) Cost of Goods Sold Deduction: using data from the IRS 2011 Statistics of Income report, this analysis divides total reported Cost of Goods Sold amounts by reported Total Receipts amounts for 2- and 3-digit NAICS code industries to arrive at the COGS deduction ratios.

    b) Compensation Deduction: using data from the IRS 2011 Statistics of Income report, this analysis divides total reported employees compensation amount (including Salaries and Wages, Compensation of Officers, Pension, Profit-Sharing, etc., Plans, and Employee Benefit Programs line items), by reported Total Receipts amounts, for 2- and 3-digit NAICS code industries to obtain the Compensation deduction ratios.

    c) Alternative Deduction: a deduction of 30% of Total Receipts.

    d) The analysis determines the highest percent deduction from the above three ratios.

11. Estimated Margin = Estimated Eligible Revenue - Estimated Deduction.

12. Estimated Taxable Margin is estimated by adjusting the Estimated Entity Margin to account only for sales made within the State of Nevada, since only these sales are taxable. This analysis uses 2011 IMPLAN Total Exports (Domestic and Foreign) as a percent of total industry output data for the State of Nevada.

13. Estimated Gross Tax Amount = Estimated Taxable Margin * 2% Tax Rate.

14. MBT credit is estimated by calculating the Modified Business Tax impact for each business entity, based on its FY 2013 wages, as provided by DETR, and wages and health care expenditures by industry as reported by the Nevada Department of Taxation. The amount of MBT credit shown in Appendix 2 does not match the total amount paid since it includes MBT amounts for impacted industries only.

15. Estimated Net Tax Amount = Estimated Gross Tax Amount - Estimated MBT Credit.