F I S C A L I M P A C T R E P O R T

SPONSOR Maestas Barnes **ORIGINAL DATE** 1/20/16 **LAST UPDATED** 2/1/16 **HB** 26

SHORT TITLE Solar Market Development Tax Credit Changes **SB**

ANALYST McIntyre

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY16	FY17	FY18	FY19	FY20		
		($3,800.0)	($3,800.0)	($3,800.0)	Recurring	General Fund

Parenthesis ( ) indicate revenue decreases

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

FY16	FY17	FY18	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
$8.8	$3.8	$3.8	$16.4	Recurring	TRD Operating Fund

(Parenthesis ( ) Indicate Expenditure Decreases)

Duplicate of SB 13

SOURCES OF INFORMATION

LFC Files

Responses Received From
Energy, Minerals and Natural Resources Department (EMNRD)
Taxation and Revenue Department (TRD)
Public Regulation Commission (PRC)

SUMMARY

Synopsis of Bill

House Bill 26 amends the Solar Market Development Tax Credit, Section 7-2-18.14 NMSA 1978, in two ways. It combines the tax credit caps for solar thermal and photovoltaic systems from $2 million and $5 million, respectively, into one aggregate cap of $5 million. The bill also extends the delayed repeal by eight years, from December 31, 2016 to December 31, 2024 to be applied through the tiered structure below:

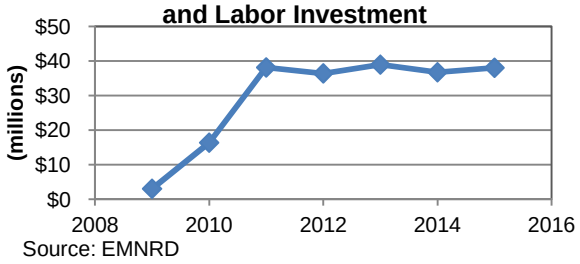
Period	Share of Purchase and Installation Costs
Prior to January 1, 2019	Up to 10 percent
After January 1, 2019 and prior to January 1, 2021	Up to 9 percent
After January 1, 2021 and prior to January 1, 2022	Up to 8 percent
After January 1, 2022 and prior to January 1, 2023	Up to 7 percent
After January 1, 2023 and prior to January 1, 2024	Up to 6 percent
After January 1, 2024 and prior to January 1, 2025	Up to 5 percent

The effective date of this bill is January 1, 2017. The delayed repeal date of this bill is December 31, 2024.

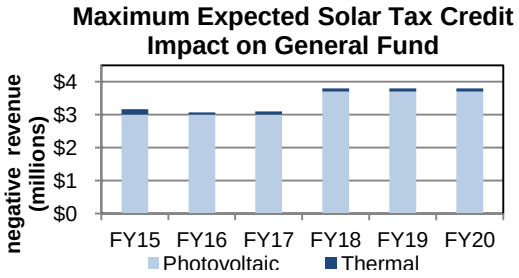
FISCAL IMPLICATIONS

Current statute caps the tax credit at $3 million for photovoltaic systems and $2 million for solar thermal systems. The tax credits for photovoltaic systems have reached the $3 million ceiling in each of the last five years, while in 2015, EMNRD certified 18 solar thermal systems for tax credits issued of approximately $68 thousand. Therefore, $1.932 million in available credits were unused for solar thermal systems. By creating an annual aggregate tax credit cap of $5 million for both systems, some homeowners and businesses who would have been denied a credit because of the current cap on photovoltaic systems could now receive the tax credit.

An average of $38 million has been spent on photovoltaic system installation and labor over the last five taxable years, according to LFC analysis of EMNRD data, as indicated in the chart on the left side below. If this trend continues, and 100 percent of tax credits awarded are fully claimed, then HB 26 could generate roughly $3.8 million in negative general fund revenue from FY18 through FY20, assuming all solar expenses qualify for the 10 percent credit, as indicated in the chart below on the right side.



Source: EMNRD



Source: LFC Analysis

Though tax credits have been awarded at the $3 million cap for photovoltaic systems, TRD notes that actual claims have stabilized around 1300 per year with total tax expenditures between $2.5 million and $2.8 million, and thereby estimates a recurring general fund impact of negative $3 million. The real total tax expenditure may be between $3 million and $3.8 million, and so the more conservative estimate of $3.8 million is adopted here.

SIGNIFICANT ISSUES

A significant investment in solar photovoltaic systems is occurring throughout much of New Mexico. New Mexico was home to 1,600 solar jobs in 2014. During 2015, approximately $31 million was invested by homeowners in solar systems. Installation of these solar systems resulted

in $6.7 million in labor costs. There were 1,065 household scale solar systems installed statewide, including rural and off-grid farms that added 6 megawatts of solar generation capacity as part of New Mexico's electric system.

There is a significant amount of residential solar generation capacity installed in most counties. In 2015 EMNRD certified 638 solar photovoltaic systems in the PNM and 167 systems in the El Paso Electric service territories, along with dozens of others in areas served by Cooperatives and municipal systems. Through certification of solar systems in 2015, EMNRD recognizes 60 firms installing solar photovoltaic systems and eight firms installing solar thermal systems.

TRD notes that the plateau in utilization raises issue as to whether the credit is still necessary. However, there has not been a drop in either the number of claims or amounts claimed, which does not indicate decreased utilization and more fulsome market saturation. It is unknown whether the reduction in credit rates, coupled with consumer's purchasing power and the costs of eligible systems, will continue to incentivize purchases of these systems in the later years in which the credit is available.

The federal solar tax credit of 30 percent for residential solar thermal and photovoltaic systems, which was set to expire on December 31, 2016, was recently extended until December 31, 2019 with a phase-down of the credit from 30 percent to 22 percent through December 31, 2022. Therefore, there is no change expected in market demand due to the impact of the federal tax credit until beyond FY20.

On August 3, 2015, the federal government unveiled the final version of the Clean Power Plan to reduce carbon emissions by 32 percent nationwide by 2030. The Environmental Protection Agency assigned each state a unique carbon emission reduction, requiring New Mexico to reduce emissions by 36 percent of 2012 levels by 2030. Currently, 8 percent of electricity generation in New Mexico comes from renewable sources.

Distributed solar generation installations allow customers to reduce their consumption of electricity from their electricity providers, thereby reducing their electric bills and utility revenues. Gross receipts tax, franchise tax, and inspection and supervision revenue are also reduced, thereby potentially decreasing local, state and PRC revenues, though consumers may redirect their savings to other purposes.

PERFORMANCE IMPLICATIONS

The LFC tax policy of accountability is not met since TRD is not required in the bill to report annually to an interim legislative committee regarding the data compiled from the reports from taxpayers taking the deduction and other information to determine whether the deduction is meeting its purpose.

ADMINISTRATIVE IMPLICATIONS

Since the tax credit is currently in place, EMNRD has an existing program to review applications and provide certifications. EMRND would update existing rules (NMAC 3.3.28) to comply with changes to the solar market development tax credit in HB 26.

TRD claims a minimal impact: GenTax must be programmed to allow for different credit percentages by year; the maximum annual aggregate will need to be updated to the new consolidated cap. Programming issues with Business Credit Manager will need to be addressed. Forms must be updated to include an installation date so that the correct tax credit percentage can be used for total credit calculation. Taxpayer instructions will need to be updated pursuant to the changes. The consolidation of the system credit caps will require clarifying language specifying if changes apply to applications submitted but not approved as of the effective date. Cross-Division Memorandums of Understanding should be updated prior to the start of the new applicability period. Regulations will need revision to accommodate the proposed changes.

DUPLICATION

This bill is a duplicate of SB 13.

TECHNICAL ISSUES

TRD notes several technical issues that exist with the current law. While not precipitated by the proposed bill and amendments these issues should be considered when analyzing the proposed amendments. First, there is an absence of claim procedures, specifically with regard to timing. The law should require the credit to be claimed for the taxable year in which the installation occurred or, alternatively the taxable year in which EMNRD issues certification. Clear claim timing will keep credits flowing smoothly and tie them more closely to the annual caps. Second, there is an inherent tension between the prohibition on systems being used for commercial or industrial purposes and the applicability of the credit to systems installed on business premises. Clarification that the systems cannot be used for commercial or industrial applications within a structure would be helpful. Finally, the bill does not define purchase and installation costs. Thus, there is an inherent lack of clarity of the expenditures to which the credit applies.

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL

The sunset date for New Mexico's Solar Market Development Tax Credit will remain at December 31, 2016.

Does the bill meet the Legislative Finance Committee tax policy principles?

1. **Adequacy**: Revenue should be adequate to fund needed government services.
2. **Efficiency**: Tax base should be as broad as possible and avoid excess reliance on one tax.
3. **Equity**: Different taxpayers should be treated fairly.
4. **Simplicity**: Collection should be simple and easily understood.
5. **Accountability**: Preferences should be easy to monitor and evaluate

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