REVENUE STABILIZATION AND TAX POLICY COMMITTEE

FINAL REPORT

New Mexico Legislative Council Service
Santa Fe, New Mexico
December 2005

CONTENTS

INTRODUCTION

Members of the Revenue Stabilization and Tax Policy Committee (RSTPC) during the 2005 interim were:

Members	Designees
Sen. John Arthur Smith, Chair	Sen. Sue Wilson Beffort
Rep. Donald L. Whitaker, Vice Chair	Rep. William "Ed" Boykin
Sen. Ben D. Altamirano	Rep. Donald E. Bratton
Rep. Janice E. Arnold-Jones	Sen. Phil A. Griego
Sen. Mark Boitano	Sen. John T.L. Grubesic
Sen. Carlos R. Cisneros	Rep. Irvin Harrison
Sen. Kent L. Cravens	Rep. Manuel G. Herrera
Rep. Anna M. Crook	Sen. Stuart Ingle
Sen. Joseph A. Fidel	Sen. Cisco McSorley
Rep. Keith J. Gardner	Sen. Steven P. Neville
Rep. Roberto "Bobby" J. Gonzales	Rep. Andy Nunez
Rep. George J. Hanosh	Rep. Greg Payne
Rep. Ben Lujan	Sen. Leonard Lee Rawson
Sen. William E. Sharer	Rep. Debbie A. Rodella
Rep. Daniel P. Silva	Sen. Nancy Rodriguez
Sen. H. Diane Snyder	Sen. John C. Ryan
Sen. James G. Taylor	Rep. Henry Kiki Saavedra
Rep. Thomas C. Taylor	Sen. Bernadette M. Sanchez
	Rep. Joe M Stell
	Rep. Don L. Tripp
	Rep. Luciano "Lucky" Varela

The RSTPC held six meetings in the 2005 interim. Three of those meetings were held at the State Capitol, while the others were held in Hobbs, Rio Rancho and Taos. Many of the committee's discussions involved maintenance of the integrity of the state's general fund, permanent funds and retirement funds. The committee also discussed several tax policy-related proposals involving the promotion of economic development, the encouragement of certain activities in the state and equitable taxation among similarly situated groups. Other proposals included administrative reforms and proposals to permit additional funding for local governments. The committee endorsed 30 tax-related proposals during the 2005 interim.

Promotion of economic development through the use of tax increment financing was a major proposal discussed by the committee. A tax increment financing mechanism is proposed to permit special tax increment financing districts to issue bonds to fund public improvements. Increased property tax and gross receipts tax collections that result from economic development would be used to finance the debt. The committee endorsed tax increment financing conceptually as a method to fund public improvements.

Other economic development-related proposals endorsed by the committee included the creation of a deduction against the gross receipts tax for the sale of chemicals consumed during the manufacturing process and a deduction against the compensating tax owed with respect to a coal-fired electric generating facility that is proposed to be located on Navajo Nation land.

Some tax incentives were proposed to the committee for reasons other than the promotion of economic development. For instance, the committee endorsed a proposal to permit a gross receipts tax deduction to aid in the costs of constructing certain public health care facilities. Another proposal was endorsed to permit a deduction from gross receipts to promote the use of electronic age verification equipment for the sale of cigarettes and alcoholic beverages. The RSTPC also endorsed a proposal to encourage the use of biomass-related equipment by providing a deduction from gross receipts for the sale of that equipment. Finally, the RSTPC endorsed a measure to encourage professional athletic competitions in the state by permitting a deduction from gross receipts for the promotion of professional athletic competitions.

The committee additionally adopted proposals for tax relief as a means of promoting equitable taxation among similarly situated groups. For example, the committee endorsed draft legislation to permit for-profit hospitals to obtain additional tax relief that was previously available only to nonprofit hospitals. The committee further endorsed draft legislation to provide a deduction from gross receipts for receipts from fee-for-service payments by health care practitioners. Those payments are currently not deductible pursuant to a deduction available for payments by managed health care providers for commercial contract services or Medicare Part C services. The committee additionally endorsed a proposal to allow a deduction available for receipts from the sale of above-ground irrigation systems to also be made available for receipts from the sale of underground irrigation systems.

The Taxation and Revenue Department proposed, and the committee endorsed, several measures to permit administrative reforms. Some of those administrative reforms include provisions to permit electronic filing of tax returns, to provide for enhanced enforcement of certain taxes and to make technical corrections to existing tax laws. The committee also adopted proposals of the New Mexico Municipal League to provide for a municipal property tax rebate for low-income homeowners; to permit the imposition of local-option compensating taxes; and to increase distributions to the State Aviation Fund.

A chart containing information on the draft legislation proposed, committee endorsements and the names of committee member sponsors of the endorsed draft legislation is included at the end of this report.

2005 APPROVED
WORK PLAN AND MEETING SCHEDULE
for the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

Members

Sen. John Arthur Smith, Chair
Rep. Donald L. Whitaker, Vice Chair
Sen. Ben D. Altamirano
Rep. Janice E. Arnold-Jones
Sen. Mark Boitano
Sen. Carlos R. Cisneros
Sen. Kent L. Cravens
Rep. Anna M. Crook
Sen. Joseph A. Fidel
Rep. Keith J. Gardner
Rep. Roberto "Bobby" J. Gonzales
Rep. George J. Hanosh
Rep. Ben Lujan
Sen. William E. Sharer
Rep. Daniel P. Silva
Sen. H. Diane Snyder
Sen. James G. Taylor
Rep. Thomas C. Taylor

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Sen. Sue Wilson Beffort
Rep. William "Ed" Boykin
Rep. Donald E. Bratton
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Sen. John T.L. Grubesic
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Sen. Stuart Ingle
Sen. Cisco McSorley
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Rep. Greg Payne
Sen. Leonard Lee Rawson
Rep. Debbie A. Rodella
Sen. Nancy Rodriguez
Sen. John C. Ryan
Rep. Henry Kiki Saavedra
Sen. Bernadette M. Sanchez
Rep. Joe M Stell
Rep. Don L. Tripp
Rep. Luciano "Lucky" Varela

WORK PLAN

The revenue stabilization and tax policy committee (RSTPC) is a statutorily created joint interim legislative committee. Pursuant to Section 2-16-3 NMSA 1978, the committee is directed to "examine the statutes, constitutional provisions, regulations and court decisions governing revenue stabilization and tax policy in New Mexico and recommend legislation or changes if any are found to be necessary . . . ".

Work Focus for 2005

Evaluate State-Sponsored Economic Development Tax Incentives

Legislation is adopted each year to provide tax incentives to promote economic development in New Mexico. During last year's interim, the RSTPC heard testimony regarding the frequency of use of existing incentives. The committee learned that there are currently few tools to monitor job growth, salary increases, income growth or increased economic activity generated by specific incentives. During the 2005 interim, the committee proposes to gather input from the economic development department, the taxation and revenue department and other agencies and organizations to better evaluate the effectiveness of those incentives in contributing to New Mexico's economy. The committee will further review whether those incentives meet general principles of good tax policy and discuss recent court decisions that might affect the provision of state-sponsored tax incentives in the future.

Review Competitive Disadvantages Attributable to the State's Gross Receipts and Compensating Tax Structure

New Mexico businesses that sell goods and services often claim that they are at a competitive disadvantage with out-of-state businesses due to New Mexico's gross receipts and compensating tax structure. Those New Mexico businesses claim that when they sell goods and services to New Mexico consumers, they must pass on to those consumers local option gross receipts taxes in addition to the five percent gross receipts tax imposed by the state. Meanwhile, the same consumers could pay only a five percent compensating tax rate if they purchase the same goods and services from out-of-state businesses. Thus, some consumers might opt to purchase those goods and services from out-of-state businesses to pay the lower tax rates. During the 2005 session, the legislature passed Senate Joint Memorial 46, which requests the taxation and revenue department to conduct a study of the competitive disadvantages realized by New Mexico businesses as a result of the state's gross receipts and compensating tax structure and present a written report of its findings and recommendations to the appropriate interim committee of the legislature. The RSTPC proposes to review and discuss the taxation and revenue department's findings and recommendations.

Study Effectiveness of Enforcement of Highway and Commercial Motor Vehicle-Related Taxes and Fees

The motor transportation division (MTD) of the department of public safety (DPS) monitors and enforces the payment of several highway and commercial motor vehicle-related taxes and fees such as the trip tax, the weight distance tax and fees for oversize and overweight permits. The MTD might encounter several challenges due to its existence as a division under the DPS and due to issues that arise from the quantity of travelers near the Mexican border. The committee proposes to discuss what those challenges might be and will examine models for divisions similar to the MTD in other border states.

Receive Updates on Streamlined Sales and Use Tax Agreement Negotiations

During the 2005 session, the legislature passed House Bill 575, which permits the secretary of taxation and revenue to participate with other states in developing a plan to simplify administration of sales and use taxes. The committee requests updates on the progress of those negotiations.

Other Tax and Fiscal Matters for Review

The committee proposes to also:

- examine economic and revenue trends;
- discuss revenue enhancement and tax relief possibilities;
- monitor severance tax revenues, including revenue and bonding authority estimates, and management of bond appropriations and expenditures;
- monitor general obligation bond capacity and indebtedness status;
- receive an update on the performance of state permanent fund investments;
- receive an update on fuel taxation on tribal lands;
- review existing tax laws for technical correction, cleanup or amendment;
- study gross receipts tax pyramiding issues;
- discuss local option gross receipts and compensating tax issues;
- receive updates on the food and medical gross receipts tax deduction;
- discuss the potential for a national retail sales tax and how the state could be affected;
- study the implementation and the effects of combined reporting;
- receive an update on tax relief provided to veterans and implementation of the veterans' property tax exemption;
- obtain updates on property tax developments;
- discuss the taxpayer bill of rights (TABOR);
- examine methods that use tax increments to finance local economic development projects;

- explore methods to fund local infrastructure projects;
- receive a report on the status of intergovernmental agreements with tribes and resulting revenue trends;
- study the effect of transportation-related taxes on state vehicle use;
- explore highway funding mechanisms; and
- conduct any other study or review of tax administration, tax laws, tax policy, public finance and revenue stabilization issues that the committee deems necessary.

APPROVED MEETING SCHEDULE

The RSTPC proposes to meet as follows:

Date	Location
June 2	Santa Fe
July 21-22	Hobbs
August 25-26	Rio Rancho
September 15-16	Taos
October 20-21	Santa Fe
November 30-December 1	Santa Fe

Revised: June 1, 2005

TENTATIVE AGENDA
for the
FIRST MEETING IN 2005
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

June 2, 2005
Room 307, State Capitol

Thursday, June 2

9:30 a.m.	**Call to Order** —Senator John Arthur Smith, Chair
9:35 a.m.	**Post-session Fiscal Summary** —David Abbey, Director, Legislative Finance Committee (LFC)
10:30 a.m.	**Review of Tax Legislation from the 2005 Session** —Kelly O'Donnell, Assistant Secretary and Director of Tax Policy, Taxation and Revenue Department (TRD)
11:15 a.m	**Review of Elimination of Gross Receipts Tax on Food** —Kelly O'Donnell, TRD —Bill Fulginiti, Executive Director, New Mexico Municipal League
12:00 noon	**Lunch**
1:30 p.m.	**Overview of Taxation on Native American Lands** —Joe Lennihan, General Counsel, TRD —Wayne Bladh, Specialist in Indian Taxation Issues, Nordhaus Law Firm, LLP
2:30 p.m.	**Proposed Desert Rock Project** —Freddy Sanches, Vice President, Sithe Global Power, LLC —Richard Minzner, Lobbyist
3:30 p.m.	**Adoption of Committee Work Plan and Meeting Schedule** —Amy Chavez, Staff Attorney, Legislative Council Service (LCS) —Pam Ray, Staff Attorney, LCS
4:30 p.m.	**Adjourn**

MINUTES
of the
FIRST MEETING
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

June 2, 2005
State Capitol, Room 307

On June 2, 2005, the first meeting of the Revenue Stabilization and Tax Policy Committee (RSTPC) for the 2005 interim was held in Room 307 of the State Capitol.

PRESENT

Sen. John Arthur Smith, Chair
Rep. Donald L. Whitaker, Vice Chair
Sen. Ben D. Altamirano
Sen. Kent L. Cravens
Rep. Anna M. Crook
Sen. Joseph A. Fidel
Rep. Keith J. Gardner
Rep. Roberto "Bobby" J. Gonzales
Rep. George J. Hanosh
Rep. Ben Lujan
Sen. William E. Sharer
Rep. Daniel P. Silva
Sen. H. Diane Snyder
Sen. James G. Taylor
Rep. Thomas C. Taylor

ABSENT

Rep. Janice E. Arnold-Jones
Sen. Mark Boitano
Sen. Carlos R. Cisneros

Staff
Amy Chavez, Pam Ray and Tim Crawford

Guests
The guest list is in the meeting file.

The chair called the committee to order at 9:40 a.m.

POST-SESSION FISCAL SUMMARY

David Abbey, director of the Legislative Finance Committee (LFC), provided an updated post-session fiscal summary for the RSTPC members. Mr. Abbey highlighted major changes in recurring general fund revenues. According to LFC estimates, recurring fiscal year 2006 general fund revenues are projected to rise up to $342 million from the fiscal year 2005 budget level. Energy-related revenues account for approximately 40 percent of the growth. Mr. Abbey also highlighted recurring general fund appropriations for fiscal year 2006. Approximately $2.1

billion of the appropriations are for public education. Additionally, $714 million is for higher education, $559 million is for Medicaid and $560 million is for other health and human services expenditures. The legislature passed legislation in 2005 to raise an additional $14.9 million. Another $11.2 million is expected to be generated by the state through enhanced audits. LFC estimates indicate the possibility that projected recurring revenue growth may be too low to support recurring expenditure levels in fiscal years 2007 through 2009. If a structural imbalance arises, it could reach up to $419 million by fiscal year 2009.

Mr. Abbey further discussed the fiscal impacts of some major pieces of tax legislation that passed during the 2005 session, including House Bill 410, the governor's tax package, and legislation affecting Medicare, public education, post-secondary education, health and human services, public safety, natural resources and economic development. Overall, total recurring general fund appropriations equal $150.8 million.

2005 TAX LEGISLATION REVIEW

Kelly O'Donnell, assistant secretary and director of tax policy, Taxation and Revenue Department (TRD), summarized 2005 legislation affecting tax policy. A major bill affecting tax policy creates the Tax Fraud Investigations Division of the TRD to investigate criminal tax fraud. Several bills affecting the personal income tax also became law, including a $2,800 refundable income tax credit for uncompensated medical expenses and an additional income tax exemption for those expenses. A $2,500 income tax exemption was also added for certain personal income tax filers. In addition, personal income tax rate reductions slowed and the nursing home bed tax credit was repealed. Heads of households are also now subject to lower income tax rates due to the passage of a bill that permits them to file in the same income tax brackets as married couples filing jointly.

Bills affecting the gross receipts tax and the compensating tax also became law. First, the legislature passed a bill to authorize the secretary of taxation and revenue to enter into the streamlined sales and use tax agreement with other states to develop a plan to simplify administration of sales and use taxes. In addition, the legislature created a gross receipts tax holiday during the first weekend in August for gross receipts from the sale of clothing, school supplies and computers. To partially offset the effects of gross receipts tax pyramiding that occurs during the sale of services for resale, the legislature passed a credit against the gross receipts tax on services sold for resale. Local governments will benefit from additional legislation giving them the authority to impose local option quality of life gross receipts taxes and eliminating a delayed repeal of the capital outlay gross receipts tax. The legislature also passed several tax incentive bills to promote renewable energy production, the provision of rural jobs and growth in the film, housing and research and development industries.

FOOD AND MEDICAL GROSS RECEIPTS TAX DEDUCTION UPDATE

Ms. O'Donnell provided the committee with the TRD's estimates of the impact of the food and medical gross receipts tax deductions on state finances. Those gross receipts tax deductions for receipts derived by retail food stores from the sale of certain food items and for receipts derived from medical service providers for certain medical receipts became effective on January 1, 2005. Through April, average deductions with respect to food gross receipts approximate $172.2 million and medical gross receipts tax deductions approximate $39.5 million. Ms. O'Donnell explained the specific rules concerning receipts that qualify for the gross receipts tax deduction. She also explained that local governments are "held harmless" from any reduction in gross receipts tax revenues by general fund distributions to the local governments.

Some gross receipts taxpayers have encountered difficulties in correctly reporting their deductions for gross receipts from food or medical services. When the deductions are overstated, local governments receive distributions that are too high. If the deductions are underreported, local governments receive distributions that are too low. Thus, a statutory penalty applies to both underreporting and overreporting. Ms. O'Donnell discussed the TRD's efforts to assist taxpayers in avoiding the penalty by providing various seminars, fact sheets and other information. Ms. O'Donnell explained that incorrect reporting of the deduction by large retailers was discovered shortly after the February 25 filing deadline. Auditors contacted those retailers and many reporting errors were resolved. Despite the TRD's efforts, Ms. O'Donnell warned that some errors persist and others may still arise. To avoid additional problems, the TRD has permitted a filing deadline extension for the gross receipts tax deduction and will adjust local distributions to correct previous reporting errors.

Bill Fulginiti, executive director of the New Mexico Municipal League, provided the committee with a survey of municipalities throughout the state with respect to the issues they have encountered as a result of the transition to the elimination of the gross receipts tax on food and on medical services. Many municipalities initially encountered reduced revenues due to low "hold harmless" distributions stemming from underreporting of deductions by large retailers and medical offices. However, revenues stabilized for most of those municipalities after working with the TRD to correct the reports. Mr. Fulginiti also noted that misreporting is more likely to occur by filers for the medical service gross receipts tax deduction than for the food tax deduction because large food retailers are better equipped to deal with the specific issues that arise from the deduction and because there are fewer large food retailers than medical service providers in the state. Medical care deduction issues also tend to be more complicated due to complex bookkeeping issues that affect medical offices.

OVERVIEW OF TAXATION ON NATIVE AMERICAN LANDS

Joe Lennihan, general counsel, TRD, provided the committee with an overview of state tax policy with respect to taxation of activities on Native American lands. He explained that the courts have used two tests to determine whether certain activities on Native American lands could be taxed by the states. One test determines whether the legal incidence of a tax falls upon tribal or nontribal members. Generally, if the lawful incidence of a tax falls upon a nontribal member, the state has authority to tax the nontribal member. If the incidence falls upon a tribal member, however, the state is less likely to have the authority to tax that person. Another test balances the economic impacts of the taxed activities on tribes, the state and federal government. Courts have held that if a tribe bears the economic impact of an activity, that activity cannot be taxed by the state. Mr. Lennihan briefly listed the tax-sharing and information-sharing agreements entered into by the state and various tribes throughout the state.

Wayne Bladh, specialist in Indian taxation issues from the Nordhaus Law Firm, LLP, elaborated on the various common law tests of the state's authority to tax various activities on tribal land. Mr. Bladh explained that a key element in determining the state's authority to tax is the legal incidence of the tax, or who is legally responsible for paying the tax. Geographical location of the activity and the political status of the party on which the legal incidence of the tax falls are additional factors to be considered. Mr. Bladh indicated that the balancing test of the economic impacts on the state, tribe and federal government previously mentioned by Mr. Lennihan is applied uniquely by different courts, and decisions in other states might not necessarily have an impact upon whether the state is legally permitted to tax an activity. He further indicated that in formulating tax policy with respect to activities on tribal lands, the state should focus on local issues and structure New Mexico taxes to achieve tax policy to achieve broader objectives, rather than simply maximizing the types of activities it can tax. He encouraged minimizing litigation between the state and tribes through negotiation and increased information-sharing.

DESERT ROCK PROJECT

Richard Minzner, lobbyist, and Freddy Sanches, vice president of Sithe Global Power, LLC, discussed the initiative to begin the Desert Rock Energy Project south of Farmington on the Navajo Nation. Mr. Minzner and Mr. Sanches explained that the Navajo Nation Council established the Dine′ Power Authority to develop Navajo energy resources. The authority selected Sithe Global Power to develop, finance, construct and operate a coal-fired electric generating facility at the proposed site near Farmington. Mr. Sanches identified objectives of the project, including improvement of the existing electrical power system in the southwestern states; delivery of competitively priced power; generation of electricity from Navajo Nation coal; relief from dependence on gas-fired power plants; and promotion of economic development for the Navajo Nation. He stated that Sithe Global Power, if the Desert Rock Project is constructed, would be the largest taxpayer on the Navajo Nation and would account for 30 percent of the Navajo Nation's budget. Taxes anticipated to be paid to the Navajo Nation include the Navajo business activity tax, the possessory interest tax and sales tax. Water fees, leases and royalties would also be paid to the Navajo Nation. State taxes, consisting of primarily compensating taxes, would also be payable to the state. Stephen Begaye, CEO of Dine′ Power Authority, stated that the combined state and tribal taxes have raised concerns that construction of the plant might not be economical. The Navajo Nation is willing to reduce the tax burden it imposes and desires that the state likewise reduce its tax burden to provide incentive for construction of the project. The Navajo Nation anticipates obtaining financing for the project by 2005 and beginning construction soon after that. Construction is anticipated to last about five years.

PROPOSED WORK PLAN AND MEETING SCHEDULE

Amy Chavez, Legislative Council Service (LCS), introduced herself, Pam Ray, Cleo Griffith and Tim Crawford as staff for the RSTPC for the 2005 interim and presented a proposed work plan and meeting schedule to the committee members. The committee adopted the meeting schedule in accordance with a master calendar prepared by the LCS upon request of the Legislative Council. The committee agreed to schedule out-of-town meetings in Hobbs, Rio Rancho and Taos, with the meeting places to be assigned to scheduled meeting days according to meeting facility availability. Remaining meetings in October and November are to be held in Santa Fe. Ms. Chavez presented a list of proposed work topics to the committee for the 2005 interim. Those topics include examination of economic development tax incentives, study of competitive disadvantages in New Mexico's gross receipts and compensating tax structure, examination of the role of the Motor Transportation Division of the Department of Public Safety in enforcing highway-related taxes and fees and review of the state's progress in entering into the streamlined sales and use tax agreement. Other topics suggested by RSTPC members for review include:

- general obligation bond capacity and indebtedness status;
- examination of the effect of transportation-related taxes on state vehicle use;
- property tax development updates;
- revenue enhancement tools and tax relief possibilities;
- highway funding mechanisms;
- methods of funding local infrastructure projects; and
- updates on the food and medical gross receipts tax deduction.

The committee adopted the work plan with the additional changes proposed by the committee members. The committee adjourned at approximately 4:25 p.m.

Revised: July 18, 2005

<u>TENTATIVE AGENDA</u>
for the
SECOND MEETING IN 2005
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

July 21-22, 2005
Mezzanine, Zia Park Racetrack
Hobbs

<u>Thursday, July 21</u>

9:30 a.m.	**Call to Order** —Senator John Arthur Smith, Chair
9:35 a.m.	**Approval of Minutes**
9:40 a.m.	**Opening Remarks** —Monty D. Newman, Mayor, City of Hobbs
10:00 a.m.	**National Enrichment Facility Status** —Marshall Cohen, Vice President, Louisiana Energy Services
11:00 a.m.	**Oil and Gas Market Update** —Kelly O'Donnell, Assistant Secretary and Director of Tax Policy, Taxation and Revenue Department (TRD)
12:00 noon	**Lunch**
1:30 p.m.	**State-Sponsored Economic Development Incentives**
	—Economic Development Tax Incentive Summary —Kelly O'Donnell, TRD
2:15 p.m.	**—Economic Development Tax Incentive Policy Analysis** —Jim O'Neill, President, O'Neill Consulting, LLC
3:15 p.m.	**—Economic Growth Attributable to Economic Development Incentives** —Rick Homans, Secretary, Economic Development Department

4:15 p.m.	—**Cases Affecting Economic Development Incentives** —Jim Eads, President and Executive Director, New Mexico Tax Research Institute

5:00 p.m.	**Recess**

Friday, July 22

8:00 a.m.	**Reconvene**
8:05 a.m.	**Local Public Infrastructure Financing** —Bill Fulginiti, Executive Director, New Mexico Municipal League —Tasia Young, New Mexico Association of Counties
9:00 a.m.	**Local Economic Development Project Financing** —Rob Dickson, Co-Chair, Governor's Task Force on Our Communities, Our Future
10:00 a.m.	**Racetrack and Casino Tax and Budget Issues** —Bruce Rimbo, President, Zia Racetrack and Casino
11:00 a.m.	**Property Tax Update** —Dr. Manuel Del Valle, Research Director, New Mexico Tax Research Institute
12:00 noon	**Lunch**
1:30 p.m.	**Veterans' Property Tax Exemption Update** —Alan Martinez, Director, State Benefits, Veterans' Services Department
2:30 p.m.	**Adjourn**

MINUTES
of the
SECOND MEETING
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

July 21-22, 2005
Zia Park Racetrack and Black Gold Casino
Hobbs

On July 21, the second meeting of the Revenue Stabilization and Tax Policy Committee (RSTPC) for the 2005 interim was held at the Zia Park Racetrack and Black Gold Casino in Hobbs.

PRESENT
Sen. John Arthur Smith, Chair
Rep. Janice E. Arnold-Jones
Sen. Carlos R. Cisneros
Rep. Anna M. Crook
Rep. Keith J. Gardner
Rep. Roberto "Bobby" J. Gonzales
Rep. Daniel P. Silva
Sen. H. Diane Snyder

ABSENT
Rep. Donald L. Whitaker, Vice Chair
Sen. Ben D. Altamirano
Sen. Mark Boitano
Sen. Kent L. Cravens
Sen. Joseph A. Fidel
Rep. George J. Hanosh
Rep. Ben Lujan
Sen. William E. Sharer
Sen. James G. Taylor
Rep. Thomas C. Taylor

DESIGNEES
Sen. Cisco McSorley (*designee for Sen. Ben D. Altamirano*)
Rep. Andy Nunez (*designee for Rep. Donald L. Whitaker*)
Sen. Leonard Lee Rawson (*designee for Sen. William E. Sharer*)
Sen. Nancy Rodriguez (*designee for Sen. Joseph A. Fidel*)
Rep. Joe M Stell (*designee for Rep. Ben Lujan*)

Staff
Amy Chavez, Tim Crawford, Cleo Griffith and Pam Ray

Guests
The guest list is in the meeting file.

CALL TO ORDER AND APPROVAL OF MINUTES

The chair called the committee to order at 9:35 a.m. The committee unanimously approved the minutes from the first meeting of the RSTPC on June 2 in Santa Fe.

INTRODUCTORY REMARKS

Monty D. Newman, mayor of the city of Hobbs, welcomed the RSTPC members to Hobbs. Mayor Newman encouraged the committee to consider earmarking certain casino revenues for municipalities. He also encouraged the committee to examine the possibility of removing the gross receipts tax on construction materials for housing projects. He additionally explained that the population of Hobbs and per capita income have declined since 1980. He mentioned that additional gross receipts taxing authority might aid in providing improvements to attract additional residents to the city. Mayor Newman also updated the committee on the renovation of a wastewater treatment plant, funded by legislative appropriation.

NATIONAL ENRICHMENT FACILITY UPDATE

Marshall Cohen, vice president of Louisiana Energy Services (LES), discussed the company's progress in the construction of the National Enrichment Facility (NEF) near Eunice. Mr. Cohen first explained the process of uranium enrichment, which will be the function of the facility. The process uses gas centrifuge technology to create low-enriched uranium, which is used to fuel commercial nuclear plants. Mr. Cohen stated that gas centrifuge technology has been used successfully in Europe for over 30 years, but has never been commercialized in the United States.

The proposed NEF is set to be designed and licensed to operate for approximately 30 years and will occupy 800,000 square feet. LES is currently awaiting a license from the Nuclear Regulatory Commission in order to begin construction. That license is expected to be issued in the spring of 2006. Mr. Cohen additionally discussed the LES's agreement with the state of New Mexico regarding disposal of the byproducts from uranium enrichment. The agreement states that on-site storage of the byproducts will be limited to a maximum of 15 years. LES will also be required to maintain financial assurance to guarantee disposal of the byproducts. The LES will not dispose of depleted uranium or construct or operate a deconversion facility in New Mexico. The LES has committed to build a private deconversion facility outside of New Mexico. The agreement also stipulates that the Department of Environment will be permitted to inspect the NEF radiation protection program; that LES will comply with the International Atomic Energy Agency standards regarding proliferation protection; and that LES will provide the NEF's physical security plan to the Department of Public Safety.

Mr. Cohen finally discussed the potential economic benefits of having the NEF in New Mexico. He stated that the facility will diversify the economic base of southeastern New Mexico. He predicted that more than 400 construction personnel will be employed by the facility during a seven-year period. Mr. Cohen also predicted permanent employment for 210 operations personnel with an average annual salary of $50,000. He further stated that LES is committed to local hiring, training and purchases for construction and operation of the facility. Mr. Cohen asked for legislative support in the continued effort to begin construction of the facility.

OIL AND GAS INDUSTRY UPDATE

Dr. Kelly O'Donnell, assistant secretary and tax policy director, Taxation and Revenue Department (TRD), provided the committee with an update on oil and gas production and sales in New Mexico. She stated that New Mexico gas production increased in the 1990s due to federal tax incentives for coal bed methane production. Most of the increase was in the San Juan Basin, which now accounts for 65 percent of total production. Annual production peaked around 1.6 trillion cubic feet in the late 1990s and began declining by about one to two percent per year. Production has stabilized around 1,560 billion cubic feet in the last two years. Total sales value of natural gas is currently at a historic peak of about $9 billion per year. The statewide average price of natural gas in New Mexico is estimated at $5.65 for fiscal year 2005, the highest on record. The July 2005 forecast assumes prices will remain high for an additional two years and gradually decline thereafter. Dr. O'Donnell stated that certain factors will affect the price of natural gas in the future, including increased demand due to summer cooling; high crude oil prices; and possible supply disruption due to hurricane season. She added that high prices might also persist until significant liquefied natural gas volumes arrive in North America.

Dr. O'Donnell further discussed trends in the production and price of oil in New Mexico. Oil production has decreased gradually over the last 25 years. The long-term decline rate stands at about one percent per year. Dr. O'Donnell predicted that the average price of oil, which is currently $45.50, is up 42 percent from last year. Overall, Dr. O'Donnell indicated that drilling in New Mexico is at a high of 79 rigs. Dr. O'Donnell listed several factors that might affect the oil market in the next few years. They include political instability in oil-exporting regions, China's and India's emergence in the world oil market, increased worldwide drilling and possible price spikes.

The oil and gas price increases are likely to have positive effects on general fund revenue. Dr. O'Donnell indicated that at the end of the year, general fund revenue will realize a 65 percent increase from the previous two years and an increase of $350 million in recurring revenue from the previous two years. Fiscal year 2005 revenues from production activity, most recently forecast at $1.55 billion, could increase to $1.7 billion when final prices are incorporated. These would be the highest revenues in history. Other revenues adding to the general fund revenues would come from corporate income tax, gross receipts tax and personal income tax revenue growth.

ECONOMIC DEVELOPMENT INCENTIVES

Dr. O'Donnell discussed the merits of offering an economic development tax in New Mexico. Dr. O'Donnell explained that primary purposes in offering such incentives include job creation and fostering specific industries. She stated that many existing credits, such as the investment credit, high-wage jobs tax credit and technology jobs credit, require job creation. However, she noted that gauging the success of those credits in creating good jobs is difficult because the data needed to assess credit success is proprietary information that the TRD is prohibited by statute from releasing to the legislature. She suggested that to improve accountability, the legislature might require companies to collect and release accountability data and amend TRD confidentiality statutes. In addition, the legislature might designate an agency to collect and analyze accountability data and provide funding for the task.

Dr. O'Donnell indicated that as accountability for economic development tax incentives becomes increasingly demanded, future tax incentives might become increasingly complex. As demands on what is expected of tax incentives become more defined, requirements and restrictions that are part of eligibility for tax incentives will lose simplicity. She noted that increased complexity brings higher costs and breeds uncertainty, which might undermine long-term growth. In addition, as current tax credits already require much administrative attention, increased accountability requirements might magnify administrative burdens.

Dr. O'Donnell summarized the provisions of several existing economic development tax credits, including the investment credit, the venture capital investment credit, the employee child care credit, the welfare-to-work credit, the rural jobs tax credit, the laboratory partnership credit, the technology jobs tax credit, the renewable energy production tax credit, the film production tax credit and the high-wage jobs tax credit.

James P. O'Neill, president, O'Neill Consulting, L.L.C., discussed basic principles of good tax policy and how the provision of economic development tax incentives complies with those principles. Mr. O'Neill indicated that high-quality revenue systems produce revenue in a reliable manner; treat taxpayers equitably; facilitate taxpayer compliance; promote fair, efficient and effective administration; minimize involvement in spending decisions; are accountable to taxpayers; and are responsive to international economic competition. Because some of the principles conflict, Mr. O'Neill stated that designing a tax system that meets all of the principles is difficult.

According to Mr. O'Neill, there are several methods that make economic development tax incentives adhere to basic tax policy principles. First, tax incentives should be properly crafted so that impacts on revenues are reasonably foreseeable. Second, incentives should treat similar potential tax credit beneficiaries equally. Ease of administration of tax incentives should also be a goal. Mr. O'Neill finally mentioned that accountability should apply to tax incentives.

Despite the widespread use of certain tax principles as a benchmark for good tax policy, Mr. O'Neill warned that the principles are not part of federal or state constitutional law. Thus, while adhering to the principles often produces better revenue and political results, deviations might sometimes be justified.

Rick Homans, secretary, Economic Development Department (EDD), discussed certain key tax incentives designed to promote economic development in the state. He stated that several new industries located operations in New Mexico because of those tax incentives. In particular, Secretary Homans attributed the location in New Mexico of Monarch Litho, Inc., Southwest Cheese, Kendal Precision Machining, Ktech, Tempur-Pedic, Merillat Industries and CI Direct to the provision of economic development tax incentives. Secretary Homans added that the EDD continues to aggressively promote tax incentives to recruit new businesses to the state. He further discussed efforts of the EDD to survey economic-based companies to determine their growth needs.

The EDD, as the result of the introduction of House Joint Memorial 11 during the 2005 legislative session, has begun an initiative to work with representatives from the TRD and other agencies and organizations as part of a task force to gather accountability data with respect to economic development tax incentives. The task force is in the process of surveying best practices in other states, studying data collection methods, considering confidentiality issues and examining methods for estimating economic impacts of incentives.

Jim Eads, president and executive director, New Mexico Tax Research Institute, summarized the findings of various analyses of economic development tax incentives. One analysis concluded that the levels of effort invested by state economic development agencies varies, but rarely sufficiently responds to policymakers who desire in-depth performance information. Another analysis found that New York has an effective mechanism of measuring incentives, which focuses on how the state might operate at a severe disadvantage without the incentives and integrates its conclusions in an economic and fiscal impact analysis. Another study found that states that offer economic development tax incentives are often less effective at attracting certain industries than states that make key public investments.

According to Mr. Eads, *Cuno v. Daimler-Chrysler*, a recent Sixth Circuit Court decision, is one of the most far-reaching court decisions involving the issue of state economic incentives. The Sixth Circuit Court held that an Ohio income tax credit was discriminatory because it was granted for investment in property located in Ohio and had the effect of penalizing a corporation already taxable in Ohio if it made later investments in a different state.

Mr. Eads indicated that some New Mexico tax credits might be threatened under the reasoning of the court in the *Cuno* decision. Although vulnerable to challenge under the reasoning of *Cuno*, the decision is binding only on states within the Sixth Circuit Court. Thus, the Tenth Circuit Court, in which New Mexico resides, might take a different view of the meaning of the United States Supreme Court's precedents and reach a different result. This would change, however, if the decision is affirmed by the United States Supreme Court. The parties to the case have petitioned for review of that decision by the United States Supreme Court. The case has not yet been accepted by the United States Supreme Court, but some analysts predict that a decision on whether the case will be reviewed will not be announced before October 2005.

In response to the *Cuno* decision, members of Congress from states in the Sixth Circuit Court have reacted with proposed legislation to specifically allow states and their political subdivisions to offer incentives. The purpose of the legislation is to affirm that a state has the authority to provide tax incentives for economic development purposes before the courts otherwise negate that power.

LOCAL PUBLIC INFRASTRUCTURE FINANCING

Bill Fulginiti, executive director, New Mexico Municipal League, discussed the role of impact fees in funding local public infrastructure projects. Mr. Fulginiti explained that the basis for development impact fees in the state is the Development Fees Act, which authorizes counties and municipalities to enact or impose development impact fees. The fees are charged by the local governments on new development to generate revenue for funding or recouping the costs of capital improvements or facility expansions necessitated by and attributable to the new development. Mr. Fulginiti emphasized that public hearings are held before the imposition of such fees.

Other sources of funding also aid in financing local public infrastructure projects. Local option gross receipts taxes, lodgers' taxes, capital outlay financing and special improvement districts are other means of providing local governments with adequate funding for their infrastructures. Mr. Fulginiti provided the committee with a table containing an itemized list of revenues raised by municipalities in 2004.

Tasia Young, legislative liaison, New Mexico Association of Counties (NMAC), discussed the effect of impact fees upon counties. She noted that with the exception of Bernalillo County, county government experience with the Development Fees Act has been limited. The impact fees administrator for Bernalillo County has reported that the impact fees program in Bernalillo County is running smoothly and that the county benefits from projects funded by impact fee revenues. Valencia County anticipates joining Bernalillo County in raising revenue through the imposition of impact fees. Ms. Young indicated that NMAC does not recommend changes to the Development Fees Act.

LOCAL ECONOMIC DEVELOPMENT PROJECT FINANCING

Rob Dickson, co-chair of the Governor's Task Force on Our Communities, Our Future, discussed the task force's recommendations to promote redevelopment in New Mexico communities. The first recommendation involves the use of tax increment financing to leverage new redevelopment growth and fund economic development projects in communities. Tax increment financing permits special tax increment financing districts to use increases in property values to pay debt on bonds issued to fund economic development projects within those districts.

The task force also advocates legislation to form neighborhood improvement districts. The neighborhood improvement districts would finance improvements within the districts by special assessments against property benefited by the improvements. Neighborhood improvement districts would bear similarities to business improvement districts created pursuant to the existing Business Improvement District Act.

RACETRACK AND CASINO BUDGET AND TAX ISSUES

Bruce Rimbo, president, Zia Park Racetrack and Black Gold Casino, discussed the improving status of the racetrack industry in New Mexico. In 1998, racing activity hit a record low as five racetracks closed. Racetrack operation has improved since then. Four racetracks currently operate in New Mexico and an additional racetrack, Zia Park, will open in September. Estimates indicate that $51 million in tax revenue attributable to racing will be raised in 2005. Mr. Rimbo also noted that purses and breeder awards for horsemen have improved significantly since 1998. In 1998, total purses and breeder awards equaled $5.7 million and rose to $46.3 million in 2005. A recent study attributed 35,700 jobs and a positive economic impact of $759 million to the New Mexico racing industry. Mr. Rimbo also discussed the favorable impact of extended gaming hours on the racing and gaming industry.

PROPERTY TAX UPDATE

Dr. Manuel Del Valle, research director, New Mexico Tax Research Institute, conducted a study comparing New Mexico's property tax rates with those of other states and presented the results of his study to the committee. Dr. Del Valle discussed current property tax obligations in New Mexico. Between 1988 and 2004, property tax obligations in New Mexico tripled, while inflation increased prices by only 60 percent. Most property tax revenues are distributed to counties, school districts and municipalities. As a result of his study, Dr. Del Valle found that residential property taxes in New Mexico are significantly lower than the United States average. This difference is especially apparent in the rural housing market. New Mexico additionally ranks among the 10 states with the lowest commercial property taxes in the country.

Dr. Del Valle also conducted a comparison of New Mexico's property tax rates with those of neighboring states. As the result of a comparison with Texas, he found that the price of Texas residential real estate is generally lower than prices in New Mexico. The low prices in Texas might stem from the significant difference in property taxes between Texas and New Mexico. Although the nominal prices of property in Texas are relatively lower than in New Mexico, the higher property taxes in Texas ultimately might raise the effective costs of residential housing in Texas. Similar results were reached as the result of a similar study for commercial property.

VETERANS' PROPERTY TAX EXEMPTION UPDATE

Alan Martinez, director of state benefits, Veterans' Services Department, discussed the administration of the recently expanded property tax exemption for honorably discharged veterans. The exemption was previously offered only to veterans who served during times of armed conflict. During the 2005 legislative session, enabling legislation was passed in response to voter approval in 2004 of a constitutional amendment to make the exemption applicable to all honorably discharged veterans. The legislation provides a mechanism for compensation of veterans who were eligible for the exemption in the 2004 tax year, but did not receive the exemption. Those veterans may claim the exemption during the 2005 tax year. Mr. Martinez explained that the veterans will be able to claim an additional $4,000 off their assessed property values during the 2005 tax year. He further attributed an increase in veteran residents in New Mexico to the availability of tax incentives provided to veterans. The Veterans' Services Department serves approximately 30,000 veterans in the state.

Revised: August 22, 2005

TENTATIVE AGENDA
for the
THIRD MEETING
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

August 25-26, 2005
Intel, Building RR 7, Room 112
Rio Rancho

Thursday, August 25

9:00 a.m.	**Call to Order** —Senator John Arthur Smith, Chair
9:05 a.m.	**Approval of Minutes**
9:10 a.m.	**Opening Remarks** —Jim Owen, Mayor, City of Rio Rancho —Terry McDermott, Government Relations Manager, Intel
9:30 a.m.	**Economic Development Incentives** —Noreen Scott, Executive Director, Rio Rancho Economic Development —Steven W. Keen, Partner, Neff & Ricci, Limited Liability Partnership —Mike Scaggs, President, Next Generation Economy
10:00 a.m.	**Produced Water Tax Credit** —John Gillis, Lobbyist, Public Service Company of New Mexico —Tom Brown, Lobbyist, Yates Petroleum Company
10:30 a.m.	**Corporate Income Tax — Combined Reporting** —Frank Katz, General Counsel, Multistate Tax Commission —J.D. Bullington, Vice President, Government Affairs, Association of Commerce and Industry
12:00 noon	**Lunch**
1:30 p.m.	**State Permanent Fund and Pension Fund Investment** —Gary Bland, State Investment Officer —Terry Slattery, Director, Public Employees Retirement Association —Evalynne Hunemuller, Director, Educational Retirement Board (ERB) —Frank Foy, ERB Investment Officer

4:30 p.m.	**Bond Capacity and Outstanding Debt** —James Jimenez, Secretary, Department of Finance and Administration
5:30 p.m.	**Recess**

<u>Friday, August 26</u>

9:00 a.m.	**Reconvene**
9:05 a.m.	**TRD Legislative Proposals** —Dr. Kelly O'Donnell, Assistant Secretary and Director of Tax Policy, Taxation and Revenue Department (TRD)
11:00 a.m.	**Food and Medical Gross Receipts Tax Deduction Update** —Dr. Kelly O'Donnell, TRD
12:00 noon	**Lunch**
1:30 p.m.	**Gross Receipts Tax Pyramiding Report** —Jim Eads, President and Executive Director, New Mexico Tax Research Institute (NMTRI) —Dr. Manuel Del Valle, Research Director, NMTRI
2:30 p.m.	**Highway Funding Mechanisms** —Rhonda Faught, Secretary, Department of Transportation (DOT) —Robert Olcott, Chief Economist, DOT
3:30 p.m.	**Local Liquor Excise Tax Distribution Issues** —Harry B. Montoya, Santa Fe County Commissioner —Tasia Young, Legislative Liaison, New Mexico Association of Counties
4:00 p.m.	**Gaming Revenue Distribution Issues** —Harry B. Montoya, Santa Fe County Commissioner
4:30 p.m.	**Adjourn**

MINUTES
of the
THIRD MEETING
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

August 25-26
Intel, Building RR 7, Room 112
Rio Rancho

On August 25, the third meeting of the Revenue Stabilization and Tax Policy Committee (RSTPC) for the 2005 interim was held at Building RR 7, Room 112 at Intel in Rio Rancho.

Present	**Absent**
Sen. John Arthur Smith, Chair	Rep. Donald L. Whitaker, Vice Chair
Sen. Ben D. Altamirano	Sen. Mark Boitano
Rep. Janice E. Arnold-Jones	Sen. Carlos R. Cisneros
Sen. Kent L. Cravens	Sen. Joseph A. Fidel
Rep. Anna M. Crook	
Rep. Keith J. Gardner	
Rep. Roberto "Bobby" J. Gonzales	
Rep. George J. Hanosh	
Rep. Ben Lujan	
Sen. William E. Sharer	
Rep. Daniel P. Silva	
Sen. H. Diane Snyder	
Sen. James G. Taylor	
Rep. Thomas C. Taylor	

Designees

Sen. Cisco McSorley (*designee for Sen. Joseph A. Fidel*)
Sen. Nancy Rodriguez (*designee for Sen. Carlos R. Cisneros*)
Rep. Luciano "Lucky" Varela (*designee for Rep. Donald L. Whitaker*)

Staff
Amy Chavez, Tim Crawford, Cleo Griffith and Pam Ray

Guests
The guest list is in the meeting file.

<u>Thursday, August 25</u>

Call to Order and Approval of Minutes

Senator John Arthur Smith, chair, called the committee to order at 9:15 a.m. The committee unanimously approved the minutes from the second meeting of the RSTPC on July 21-22 in Hobbs.

Introductory Remarks

Jim Owen, mayor of the city of Rio Rancho, welcomed members of the RSTPC to Rio Rancho and expressed his appreciation for the state legislature and his desire to cooperate with the legislature with respect to future projects in Rio Rancho. Terry McDermott, government relations manager for Intel, welcomed members of the RSTPC to the Intel facility. He noted that the Intel facility in Rio Rancho employs 5,000 employees and 2,500 independent contractors and accounts for a $302 million annual payroll. He also discussed Intel's contributions to surrounding community colleges, Rio Rancho High School, Next Generation Economy, Explora Children's Science Museum, the National Hispanic Cultural Center and the United Way. RSTPC members discussed the contribution that plants like the Intel facility might have as an additional gross receipts tax source.

Economic Development Incentives

Noreen Scott, executive director, Rio Rancho Economic Development (RRED), discussed economic development in New Mexico. She explained that a significant part of Rio Rancho's economy employs people to produce goods and services. As that sector of the economy grows, retail leakage occurs and income growth occurs. RRED estimates that 6,000 economic- development-based jobs exist in Rio Rancho. Ms. Scott warned, however, that some of those jobs might be threatened by outsourcing of labor to foreign companies.

Stephen Keene, partner, Neff and Ricci, L.L.P., discussed the effects of tax pyramiding on New Mexico manufacturing industries. Tax pyramiding occurs when a transaction tax is imposed on the inputs of a process and then is again imposed on the final output. The result is the imposition of a "tax on a tax". As a result of such pyramiding, manufacturing companies often bear a high tax burden because of their dependency on several inputs. Mr. Keene explained that New Mexico taxes inputs more frequently than other states and thus, the additional taxes due to pyramiding in New Mexico are among the highest in the country.

Mike Scaggs, president, Next Generation Economy (NGE), discussed NGE's role in creating a higher standard of living in New Mexico by nurturing an entrepreneurial economy powered by human creativity. NGE fosters growth in optical, biological science, artisan, microsystems, government service, aerospace and digital media industries. Mr. Scaggs discussed the stages that a company undergoes in manufacturing products in those industries. The stages include research and development, application of research to goals, business formation, manufacturing and distribution. Mr. Scaggs asked the committee to examine how some of the most successful states in the area of manufacturing treat manufacturing inputs. He suggested that such states should be used as benchmarks for policy formation with respect to manufacturing in New Mexico.

Questions and comments from the committee members addressed:

- whether the manufacturing industry should be regulated to promote additional economic development in manufacturing;
- the impact of recently passed legislation to reduce gross receipts tax pyramiding;
- the role of property costs and infrastructure proximity in promoting economic growth;
- the challenge of attracting manufacturing businesses that seek long-term reliability from tax systems; and
- whether reduced income tax rates play a significant role in attracting manufacturing companies to the state.

Produced Water Tax Credit Proposal

John Gillis, lobbyist, Public Service Company of New Mexico, and Tom Brown, lobbyist, Yates Petroleum Company, proposed that the RSTPC endorse legislation to provide tax credits for investments in cleaning water produced from oil and gas drilling and production. They noted that similar legislation was endorsed by the committee during the 2004 interim with respect to House Bill 197, introduced in 2005. The legislation introduced in 2005 provided a corporate income tax credit for the gathering, transporting or treating of produced water for disposition in the generation of electricity. The legislation proposed by Mr. Gillis and Mr. Brown for the current interim would provide a credit to operators of oil or gas wells who deliver produced water to the Interstate Stream Commission at the Pecos River in compliance with the Pecos River Compact and the New Mexico Water Quality Act and applicable state rules and federal laws.

Questions and comments from the committee members addressed:

- whether current companies have attempted to clean produced water;
- who owns produced water produced by oil and gas producers; and
- the potential number of claims of the proposed credit.

Mandatory Combined Reporting

Frank Katz, general counsel, Multistate Tax Commission (MTC), summarized the MTC's viewpoints with respect to the debate on mandatory combined reporting for corporate income tax purposes. He explained that combined reporting accounts for and apportions the total income earned by a group of commonly owned or controlled corporations that form the operation of a unitary business. A unitary business is composed of subdivisions of a business that are substantially interdependent and share flows of value.

Mr. Katz stated that mandatory combined reporting would result in better apportionment of income and would ensure that income earned in New Mexico would be taxed in New Mexico. He warned that under the current system, companies might continue to shift income to other states with lower tax burdens, even if that income is primarily earned in New Mexico. He further stated that combined reporting has been successfully implemented in other states and that New Mexico should follow suit. He referenced House Bill 320, which was introduced during the 2005 legislative session and which would have mandated combined reporting. Mr. Katz stated that mandated combined reporting could control income shifting, and thus result in a more accurate measure of income. Sixteen states currently require combined reporting. Neighboring states that mandate combined reporting include Arizona, Colorado and Utah. Mr. Katz suggested that New Mexico should become uniform with these states.

J.D. Bullington, lobbyist, Association of Commerce and Industry (ACI), and Doug Cox, president of ACI's Tax Commission, expressed the ACI's viewpoint against mandatory combined reporting. ACI considers mandatory combined reporting as a tax increase that creates uncertainty and unpredictability in tax structure. Mr. Cox stated that some companies have located in New Mexico in expectation of a certain filing method. ACI holds that requiring combined filing would force new requirements on corporations without warning. ACI also objects to mandatory combined filing because it views such filing as an additional burden of tax compliance. Mr. Cox stated that tax planning that occurs under the current system benefits business and should not be viewed as a problem.

Mr. Keene, provided the committee with statistics regarding combined corporate income tax reporting. He stated that currently, 16,000 corporate taxpayers in New Mexico file their corporate income tax returns on a separate basis, while 370 file combined returns and 866 file federal consolidated returns. Mr. Keene concluded that approximately 98 percent of the corporate taxpayers in New Mexico could be adversely affected by mandating combined reporting. He stated that New Mexico currently has a satisfactory corporate tax system in place and should avoid implementing a new tax system of which state agencies are not completely familiar.

Kelly O'Donnell, assistant secretary and tax policy director, Taxation and Revenue Department (TRD), stated that the TRD does not have a position on combined reporting, but noted in agreement with Mr. Katz that 98 percent of corporate income tax filers would probably not be affected by legislation to mandate combined reporting, since many current separate filers are small corporations that do not have subsidiaries.

Questions and comments from the committee members addressed:

- the modified combined reporting system of Colorado;
- which companies would be affected by mandatory combined reporting;
- the potential fiscal impact of mandatory combined reporting in the state;
- additional states that have combined reporting mechanisms;
- different methods of approaching combined reporting;
- whether combined reporting would prevent businesses from entering New Mexico; and
- the possibility of requiring combined reporting but reducing corporate income tax rates.

State Investment Funds Update

Gary Bland, state investment officer, discussed the performance of funds managed by the State Investment Council (SIC). For the fiscal year ended June 30, 2005, funds managed by the SIC realized an approximate 9.6 percent return, which exceeded its 9.3 percent benchmark. A blended benchmark of the Standard & Poor's 500 and Lehman Brothers Aggregate Bond Index was 6.5 percent. Final performance figures are awaiting private equity market valuation updates, which include approximately 135 limited liability partnerships. The state's permanent funds had a June 30, 2005 market value increase of $730 million. $587.4 million of that increase is attributable to a market increase in the Land Grant Permanent Fund (LGPF); $136.5 million is attributable to an increase in the Severance Tax Permanent Fund (STPF); and $6.6 million is attributable to an increase in the Tobacco Settlement Permanent Fund (TSPF).

State Investment Officer Bland also discussed the status of distributions from funds administered by the SIC. He noted that the Constitution of New Mexico authorizes a 5.8 percent distribution from the LGPF in fiscal years 2005 through 2012 and a reduced distribution of 5.5 percent from fiscal years 2013 to 2016. If the average year-end market values of the fund for the immediately preceding five calendar years is less than $5.8 billion, distributions will not be made from the fund. For fiscal year 2007, the total expected distribution from the LGPF is $438.4 million with 83 percent, or $363.9 million, allocated to public schools. The total distribution for fiscal year 2006 is expected to equal approximately $424.4 million, with 83 percent, or $353.9 million, allocated to public schools.

State Investment Officer Bland presented a summary report of the SIC's investment holdings. He noted that 71.18 percent of the managed net assets of the SIC are comprised of domestic and international equities. The remainder of the SIC's managed net assets are comprised of fixed income and cash. Mr. Bland provided a further breakdown of the assets comprising each of the investment holdings with respect to the LGPF, STPF and TSPF.

Evalynne Hunemuller, director, Educational Retirement Board (ERB), discussed the ERB's role as the state's largest retirement system. New Mexico's educational retirement system is comprised of 67,200 active members, 27,000 retirees and 33,000 inactive members. The payroll contributed by active members to the Educational Retirement Fund (ERF) during 2005 is $2.2 billion.

Ms. Hunemuller discussed some of the challenges of maintaining the ERF and distributing benefits to retirees. Since 1993, active membership has increased at approximately 1.8 percent per year and retiree numbers have increased by about 4.8 percent each year. There are currently 2.6 active members for each retiree. Ms. Hunemuller noted that retirees are living longer and collecting pensions for an increased period of time. Contribution levels have increased slightly to 17.075 percent in 2005 from 16.25 percent in 2004. Senate Bill 181, which became law in 2005, increased employer and employee contributions to the ERF as a percentage of total teacher payroll.

The ERB proposes to increase the returns of investment of the ERF by further diversifying its portfolio. Ms. Hunemuller proposed that the legislature implement a three- to five-year review process to make necessary changes to the funding mechanism for the ERF.

Frank Foy, investment manager, ERB, discussed the restructuring in 2002 of the ERF investment portfolio. He also provided the committee with information regarding asset growth in the ERF. In June 30, 2005, the fund assets approximated $7.4 billion. He anticipates that the fund will continue to grow. Mr. Foy discussed the returns of funds invested in domestic equities, international equities, core fixed income, high-yield securities and real estate investment trusts.

Mr. Foy further discussed the effect that recently passed legislation to permit the ERB to invest in alternative investments might have upon the ERB. He stated that the ERB staff has met with vendors and is interested in hedge fund, private equity and real estate investments. In addition, the ERB hired a new investment consultant to conduct an asset and liability study during 2006 to assist the ERB in determining asset classes in which to invest.

Terry Slattery, director, Public Employees Retirement Association (PERA), discussed the allocation of the assets of the funds administered by the PERA and briefed the committee on the performance of those funds. According to Mr. Slattery, 79 percent of the funds are invested in domestic equity pools, while 21 percent are invested in international equity pools. He further provided the committee with an overview of the amounts of funds invested with specific investment managers and discussed their performance. He discussed the returns of PERA's investments, all of which either exceeded or met target returns. Over the next 10 years, Mr. Slattery expects that cumulative returns will continue to outperform target returns.

Questions and comments from the committee members addressed:

- distributions that might be made from the corpus of SIC funds;
- amounts invested by third-party investors with respect to SIC funds;
- the lack of use of legislatively granted authority to invest in hedge funds;
- rates of return on cash and cash equivalents with respect to SIC funds;
- the effect of increased retirements on valuation of retirement fund assets;
- whether increased salaries affect the quantity of retirees that withdraw retirement benefits from retirement pension funds;
- amounts paid to retirees from the ERF;
- underperformance of certain money managers hired by the ERF;
- the average retirement age of educational retirement beneficiaries;
- constitutional provisions affecting the composition of retirement funds; and
- the potential impact of not changing contributions.

Bond Capacity and Outstanding Debt

James Jimenez, director, Department of Finance and Administration (DFA), provided the committee with an overview of bond capacity available for the 2006 legislative session. Mr. Jimenez emphasized the opportunities presented by strong economic growth and high oil and gas prices in New Mexico. According to DFA estimates, between $541 million and $590 million will be available to fund new capital outlay projects during the 2006 session. The DFA estimates that funding capacity is composed of $142.8 million in general obligation bond capacity, $198 million in net new severance tax bond capacity and between $200 million and $250 million from the general fund. Mr. Jimenez stated that those estimates will be updated before the session.

Net senior severance tax bond capacity is expected to approximate $198 million. Supplemental severance tax estimates amount to $162.8 million. Supplemental severance tax bonding will primarily be used for public school capital outlay projects. Severance tax bond capacity is projected to increase slightly in fiscal year 2006 and decrease slightly during the following three years. Such capacity, however, is not expected to fall below $350 million during that time span.

Mr. Jimenez provided the committee with data regarding capital financing during fiscal year 2005. The DFA issued $521 million in bonds and notes during fiscal year 2005. This level of financing could support over 1,000 projects statewide. During the 2005 legislative session, $470 million funded 2,600 capital outlay projects throughout the state. Approximately $99.8 million was used to fund quality of life projects and $97.1 million funded public education projects. In addition, $75.8 million funded water projects and $54.9 million was allocated to transportation projects. Mr. Jimenez also provided information on amounts obtained by the Governor's Finance Council for economic development, energy, health, housing and water projects during the 2005 session.

Mr. Jimenez further discussed improvements in capital outlay project accountability. For instance, balances on capital outlay projects more than five years old have been reduced from over $54 million in FY 2003 to approximately $12.6 million. Over $11 million has also been reverted to the Severance Tax Bonding Fund. The DFA pledges to identify additional projects that can be closed out, reauthorized or reverted. The DFA's other goals include locking in high oil and gas prices for future bonding capacity and exploring options to use bonding alternatives to reduce general fund obligations for the ERB.

Questions and comments from the committee members addressed:

- how capital outlay funding might be used to address health care issues;
- whether investment in GRIP 2 highway projects would be a funding priority;
- whether public defender and court projects will be funded;
- the effect of unanticipated construction costs on capital outlay projects; and
- the possibility of exploring projects to benefit elderly populations.

Friday, August 26

Taxation and Revenue Department (TRD) Legislative Proposals

Dr. O'Donnell provided the committee with an overview of the TRD's legislative proposals for the 2006 legislative session. The TRD's legislative agenda is centered on accountability, weight-distance tax initiatives, taxpayer compliance, uniformity of state tax law with federal law, the Uniform Unclaimed Property Act and cigarette tax compliance.

As part of its effort to promote accountability, the TRD proposes to make tax credits in excess of $10,000 public record. Currently, only refunds over $10,000 are public record. Dr. O'Donnell noted that such an effort could improve transparency and accountability in tax incentives.

The TRD further proposes to provide the Motor Transportation Division of the Department of Public Safety with compliance tools to better enforce weight-distance taxes. The TRD's proposed legislation would permit vehicles that are not tax compliant to be detained. Penalties would also be imposed for failure to stop at ports of entry; for carrying overweight loads; for operating without oversize-overweight permits; and for failure to carry appropriate identification cards, log books and records.

Other legislation proposed by the TRD would repeal Sections 7-16A-8 and 7-16A-10

NMSA 1978, which permit farmers and contractors to buy clear diesel for off-road use. In addition, the TRD proposes to extend penalty and interest free payment windows from 30 to 180 days and to apply managed audit penalty waivers to penalties imposed with respect to reports of food and medical deductions against the gross receipts tax. The TRD also will promote legislation to increase the efficiency with which abandoned property is located and disposed.

Finally, the TRD will support legislation to amend cigarette tax seizure provisions to allow the TRD to destroy seized cigarettes that are not redeemed within 30 days by the person from whom the cigarettes were seized. That legislation would additionally increase information reporting requirements for distributors and increase penalties for noncompliance with cigarette tax laws.

Questions and comments from the committee members addressed:

- the need to ensure that certain taxpayer information remains confidential;
- the success of the TRD in enforcing the cigarette tax;
- whether school bus contractors are eligible for tax deductions;
- the effect of cigarette taxes on cigarette consumption;
- how to avoid encouraging the purchase of cheaper cigarettes stemming from increased cigarette taxes; and
- how much revenue is generated in penalties associated with weight-distance tax enforcement at the border regions of New Mexico.

Food and Medical Gross Receipts Tax Deduction Update

Dr. O'Donnell discussed TRD data obtained with respect to claims of the deductions against the gross receipts tax on the sale of food and medical services. Dr. O'Donnell explained eligibility for the deduction and the provisions that hold local governments harmless from the effects of providing the deduction. She also explained that the legislation implementing the deduction also provided for stiff penalties for incorrect reporting.

Dr. O'Donnell noted that costs to the state of providing the deduction with respect to food sales have been higher than originally anticipated by the TRD. Claims of the gross receipts tax deduction on sales of food are 25.6 percent higher than anticipated. Payments to local governments to hold them harmless from the provision of the deductions are 36 percent higher than anticipated. Much of the problem in predictability stems from incorrect reporting earlier this year. To accommodate retailers that encountered difficulties in reporting deductions, the TRD permitted a filing deadline extension with respect to the deduction. Despite initial difficulty, the TRD predicts that claims of deductions will stabilize.

The TRD has found that higher-than-predicted payments to local governments with respect to the hold harmless provisions of the gross receipts tax deductions with respect to food and medical services have increased the cost of those deductions. Payments to local governments to hold them harmless from the costs of the deductions have exceeded TRD's expectations. Hold harmless payments to local governments have exceeded TRD's original estimates by $908,112.

Questions and comments from the committee members addressed:

- the benefit of increased deduction claims to taxpayers;
- whether the TRD has considered the impact on gross receipts tax revenues of reduced sales due to reduced disposable income;
- the portion of gross receipts taxes paid by out-of-state visitors;
- promotion of a customer-friendly culture at the TRD;
- the success of the gross receipts tax holiday held in August; and
- how other states administer sales tax deductions or exemptions for food sales.

Gross Receipts Tax Pyramiding Update

Jim Eads, president and executive director, New Mexico Tax Research Institute (NMTRI), and Dr. Manuel Del Valle, research director, NMTRI, provided the committee with a report regarding gross receipts tax pyramiding in New Mexico. Dr. Del Valle explained that the gross receipts tax has been a growing source of state revenues. Dr. Del Valle estimated that since 1989, gross receipts tax collections have increased by 50 percent. More than 31 percent of general fund state revenues and 40 percent of both state and local revenues are collected through imposition of the gross receipts tax.

Dr. Del Valle explained that gross receipts tax pyramiding occurs when the gross receipts tax levied at early stages of production is shifted forward. The tax eventually becomes the base for subsequent price increases and final purchasers pay a higher price as a result of the tax imposed on the tax.

The NMTRI conducted a study of the extent to which pyramiding occurs in New Mexico. The study measured amounts spent by 16 different industries on business inputs. The study then measured amounts saved by those industries as the result of statutory relief from taxation of those inputs. Among the 16 industries studied, the NMTRI found that gross receipts taxes attributable to pyramiding approximated $748.6 million. Overall, statutory relief to industries reduced pyramiding costs to those industries by 36.3 percent.

Questions and comments from the committee members addressed:

- methods to reduce gross receipts tax pyramiding;
- the ability of industries to deduct gross receipts tax pyramiding costs as business expenses; and
- factors that account for gross receipts tax pyramiding differences between industrial sectors.

Gaming Revenue Distribution Issues

Julian Barela and Hutch Miller, Santa Fe County, provided the committee with an overview of the expenditures related to tribal operations incurred by Santa Fe County. During fiscal year 2005, Santa Fe County spent $443,699 on tribal projects within the county. The county spent approximately $15,450 on DWI programs; $111,634 for fire departments; $265,000 for the Project and Facilities Management Department; $50,781 for solid waste and traffic engineering; and $833 for animal control. Mr. Barela and Mr. Miller also discussed memoranda of understanding entered into by Santa Fe County with tribes within the county, including the Pueblos of Tesuque and Santa Clara. The memoranda state agreements between the county and tribes to cooperate in developing mutually acceptable solutions to meeting various capital and program needs in tribal areas. Santa Fe County proposes that the 2006 legislature pass legislation to redistribute gaming revenues to local governments for tribal wastewater projects, roads, health and DWI programs, community centers, senior services and emergency services.

Questions and comments from the committee members addressed:
- the amount of gaming revenues the county requests for redistribution; and
- the distribution of *Aamodt* settlement revenues.

Local DWI Program Distribution Issues

Dr. Tasia Young, legislative liaison, New Mexico Association of Counties, and Rob Mitchell, DWI Solutions Committee, San Juan County, suggested means of strengthening funding for local DWI programs. Mr. Mitchell stated that DWI is a significant public health and human services cost to New Mexico in terms of quality of life and financial loss. In 2003, the death rate per 100,000 population in New Mexico was 11.4 compared to a national rate of 5.9 and the single most common contributing factor in fatal crashes was alcohol. The Division of Governmental Research at the University of New Mexico estimates that alcohol-related accidents cost the state $1,005,333,000 in 2003. Mr. Mitchell explained that when the Local DWI Grant Fund was created that year, financial support was granted to counties for the creation and maintenance of DWI programs unique to local needs. He stated that such programs reduced DWI occurrences, injuries and fatalities.

Mr. Mitchell indicated that despite the success of DWI programs funded by the Local DWI Grant Fund, funding to local programs has been reduced by more that $2.3 million annually since fiscal year 2004. He asked the committee members to consider providing additional DWI grant money to counties to alleviate the impact of escalating program costs and the consequential reduction in services experienced during the last three years.

Questions and comments from the committee members addressed:
- the efforts of counties to fund DWI programs;
- how counties in different areas of the state have addressed DWI prevention;
- whether excessive requirements hamper the ability of DWI programs to operate effectively;
- whether improved reporting mechanisms for counties should be adopted;
- whether counties duplicate services;
- whether local option liquor excise taxes have been used for financing DWI programs;
- the performance of DWI programs in rural counties; and
- which counties have the greatest funding needs for DWI issues.

Highway Funding Mechanisms

Rhonda G. Faught, secretary, Department of Transportation (DOT), and Robert Olcott, chief economist, DOT, provided the committee with an overview of funding mechanisms for highways throughout the state. Mr. Olcott discussed the role of Governor Richardson's Investment Proposal (GRIP) in funding highway projects throughout the state. He also noted that the state has an opportunity to obtain a 30-percent increase in federal funding. To obtain such funding, however, the state will be required to increase state revenue dedicated toward federal matching funds by $15 million to $20 million per year.

Mr. Olcott additionally discussed the composition of the State Road Fund. He noted that 55 percent of the fund is composed of fuel tax revenues, while 24 percent is composed of heavy vehicle taxes and the balance is funded by Motor Vehicle Division registration and license fees. Gasoline price increases and continued high prices have sparked concern that the road fund might be exposed to significant risk. Mr. Olcott explained that in addition to jeopardizing road fund revenue, high fuel prices could also raise costs of providing services and infrastructure. For instance, the price of oil strongly impacts the cost of road construction and maintenance since asphalt is comprised of oil and aggregate. As the price of oil increases, the cost of asphalt increases. High fuel prices also drive up the cost of operating heavy equipment.

Secretary Faught mentioned federal and state energy conservation initiatives and the impact they might have on the fund. Although she expressed the importance of supporting conservation, she stated that such initiatives should be balanced with stabilizing funding needs for transportation. She suggested exploration of alternatives such as mass transit. Such alternatives might benefit the state's aging, physically disabled and economically disadvantaged populations.

The DOT has cooperated with the TRD and the Motor Transportation Division of the Department of Public Safety to identify issues that might contribute to the adequacy and stability of the State Road Fund. Proposals stemming from the departments' discussions include the imposition of penalties for failure to file timely weight-distance taxes; penalties for violations of tax identification permit provisions; and consideration of imposing specific tax rates on specific taxes imposed on certain fuels pursuant to the Alternative Fuel Tax Act.

Questions and comments from the committee members addressed:

- highway funding relative to funding in previous years;
- the impact of gasoline tax revenues on federal matching funds;

- increased highway project costs attributable to the price of oil and gas;
- whether the supply of oil can meet New Mexico's transportation needs;
- regulation of the oil and gas industry;
- the impact of cement shortages on highway project costs;
- whether technology advances have reduced highway construction costs;
- whether the state has invested in small shuttle buses for elderly residents; and
- the impact that an increased gasoline tax might have on the State Road Fund.

The committee adjourned at 3:45 p.m.

Revised: September 14, 2005

TENTATIVE AGENDA
for the
FOURTH MEETING
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

September 15-16, 2005
Taos Convention Center
Taos

Thursday, September 15

9:30 a.m. **Call to Order**

9:35 a.m. **Approval of Minutes**

9:40 a.m. **Opening Remarks**
—Mayor Bobby F. Duran, Town of Taos

9:55 a.m. **Intergovernmental Council Status**
—Barbara Wiard, Vice Chair, Intergovernmental Council

10:25 a.m. **Kit Carson Electric Cooperative Update**
—Luis Reyes, Chief Executive Officer, Kit Carson Cooperative

10:45 a.m. **Recycling Equipment Tax Exemption**
—Marlene Feuer, Director, New Mexico Recycling Coalition
—English Bird, Executive Director, New Mexico Recycling Coalition

11:15 a.m. **Tax Expenditure Budgets**
—Jim Eads, President and Chief Executive Officer, New Mexico Tax Research Institute

12:00 noon **Lunch**

1:30 p.m. **New Mexico Association of Counties Proposals**
—Dr. Tasia Young, Legislative Liaison, New Mexico Association of Counties (NMAC)

2:00 p.m. **DWI Program Funding Follow-Up**
—Dr. Tasia Young, NMAC
—Vickie Evans, Local Government Division, Department of Finance and Administration

2:30 p.m. **Tax Credits for Private School Tuition**
—Troy Williamson, Executive Director, Educate New Mexico
—Ron Donkersloot, New Mexico Association of Nonpublic Schools
—Dr. Moises Venegas, Executive Director, Albuquerque Partnership

3:30 p.m. **Gross Receipts Tax Deduction for Hospitals**
—Cindy West, Lobbyist
—Dan Weaks, New Mexico Hospital Association
—Fred Woody, Carlsbad Medical Center

4:00 p.m. **Recess**

<u>Friday, September 16</u>

9:00 a.m. **Reconvene**

9:05 a.m. **Tax and Expenditure Limit Overview**
—Bert Waisanen, Senior Policy Specialist, Fiscal Affairs, National Conference of State Legislatures

10:00 a.m. **Streamlined Sales Tax Agreement Negotiation Update**
—Dr. Kelly O'Donnell, Assistant Secretary and Tax Policy Director, Taxation and Revenue Department (TRD)

11:00 a.m. **Severance Tax Permanent Fund Distributions**
—Doug Williams, Economist, Legislative Council Service

12:00 noon **Lunch**

1:30 p.m. **Motor Transportation Division Enforcement Issues**
—John Denko, Secretary, Department of Public Safety (DPS)
—Captain Ron Cordova, Motor Transportation Division, DPS
—Dr. Kelly O'Donnell, Assistant Secretary and Tax Policy Director, TRD
—Andres Aragon Viamonte, Deputy Secretary, Programs and Infrastructure, Department of Transportation (DOT)
—Vince Martinez, Deputy Secretary, Business Management and Program Support, DOT
—Robert Olcott, Chief Economist, DOT

3:00 p.m. **Adjourn**

MINUTES
of the
FOURTH MEETING
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

September 15-16
Taos Convention Center
Taos

On September 15, the fourth meeting of the Revenue Stabilization and Tax Policy Committee (RSTPC) for the 2005 interim was held at the Taos Convention Center in Taos.

Present

Rep. Janice E. Arnold-Jones
Sen. Mark Boitano (9/16)
Sen. Carlos R. Cisneros
Rep. Anna M. Crook
Rep. Keith J. Gardner
Rep. Roberto "Bobby" J. Gonzales
Rep. Ben Lujan (9/16)
Rep. Daniel P. Silva (9/15)
Sen. James G. Taylor (9/15)
Rep. Thomas C. Taylor

Absent

Sen. John Arthur Smith, Chair
Rep. Donald L. Whitaker, Vice Chair
Sen. Ben D. Altamirano
Sen. Kent L. Cravens
Sen. Joseph A. Fidel
Rep. George J. Hanosh
Sen. William E. Sharer
Sen. H. Diane Snyder

Designees

Sen. Sue Wilson Beffort (*designee for Sen. H. Diane Snyder*)
Sen. John T.L. Grubesic (*designee for Sen. Ben D. Altamirano*)
Sen. Nancy Rodriguez (*designee for Sen. John Arthur Smith on 9/15*)
Sen. John C. Ryan (*designee for Sen. Kent L. Cravens)*
Rep. Henry Kiki Saavedra (*designee for Rep. Donald L. Whitaker*)
Rep. Joe M Stell (*designee for Rep. George J. Hanosh*)
Rep. Luciano "Lucky" Varela (*designee for Rep. Ben Lujan on 9/15*)

(Attendance dates are noted for those members not present for the entire meeting.)

Staff
Amy Chavez, Tim Crawford, Cleo Griffith and Pam Ray

Guests
The guest list is in the meeting file.

Thursday, September 15

Call to Order and Approval of Minutes

Representative Roberto "Bobby" J. Gonzales and Senator Carlos R. Cisneros acted as co-chairs for the fourth meeting of the Revenue Stabilization and Tax Policy Committee (RSTPC) in Taos. Senator Cisneros called the committee to order at 9:40 a.m. The committee unanimously approved the minutes from the third meeting of the RSTPC on August 25-26 in Rio Rancho.

Introductory Remarks

Bobby Duran, mayor, Town of Taos, welcomed the committee members to Taos. Charlie Gonzales, mayor, Village of Questa, also welcomed the committee members. Mayor Gonzales encouraged continued support for transportation systems throughout the state and offered Questa's support in developing transportation programs. Mayor Gonzales also discussed local needs for the Village of Questa. He noted that the village will seek an appropriation for replacement of a wastewater treatment plant.

Barbara Wiard, mayor pro tem, Village of Taos Ski Valley, and co-chair, Intergovernmental Council, explained the role of the Intergovernmental Council in northern New Mexico. Mayor Pro Tem Wiard explained that the council is composed of 13 members, including local and tribal officials from throughout northern New Mexico. The mission of the council is to enhance northern New Mexican communities, foster educational opportunities and provide for the social and economic well-being of residents in northern New Mexico. Mayor Pro Tem Wiard provided the committee with an overview of projects undertaken by the council, including projects in the Eagle Nest Lake area and projects to support local pediatric clinics.

Jean Marquardt, executive director, Taos Center for the Arts, discussed the role of the center in providing community theater performances to the Taos area. She also discussed the center's efforts in providing programs for schoolchildren in the Taos area. She asked the committee members to consider providing support to the center for expansion of the local theater in Taos.

Alex Abeyta, El Valle de Los Ranchos Water and Sanitation District, discussed the district's necessity to find funding for various capital projects. Such projects include wastewater system improvements and the purchase of water rights.

Questions and comments from the committee members addressed:

- the amount of appropriation that might be necessary to replace the Questa wastewater treatment plant;
- who would be served by additional transit services;
- the distribution of the lodger's tax in Taos County;
- whether Taos Ski Valley obtained any part of the appropriation to the Tourism Department for advertising;
- the proposed commuter rail system;
- whether water and sanitation districts can obtain project financing through the New Mexico Finance Authority; and
- potential water rights conflicts between municipalities and pueblos.

Kit Carson Electric Cooperative Update

Luis Reyes, chief executive officer, Kit Carson Electric Cooperative, provided the committee with an update of its activities in Taos, Colfax and Rio Arriba counties. The cooperative engages in propane, Internet, telecommunications and economic development activities. The cooperative has also created a call center, a regional command center and a solar manufacturing plant. The cooperative provides broadband Internet services to Penasco, Ojo Caliente and surrounding areas. It also has partnered with the Taos Municipal School District to provide voice service and broadband applications to all schools within that district.

Mr. Reyes provided the committee members with statistics regarding its provision of propane. The cooperative has 3,016 propane customers and seven competitors. The cooperative's bulk storage capacity stands at 310,000 gallons. The cooperative sells about 2.4 million gallons of propane annually. Mr. Reyes stated that a mission of the cooperative's propane initiative is to continue to preserve safety by ensuring safe installations. Another mission of the cooperative's propane initiative is to use financial tools to keep propane prices competitive. Mr. Reyes stated that the cooperative currently has the lowest propane prices in northern New Mexico. As a result of the low prices, cooperative representatives have estimated that northern New Mexico has experienced a 43 percent reduction in the market cost of propane during the last heating season.

Kit Carson Electric Cooperative has also participated in several renewable energy programs in northern New Mexico. The cooperative participates in green tariff and net metering initiatives. It has also conducted studies on renewable energy sources, including wind generation, solar and photovoltaic energy sources.

Finally, Mr. Reyes discussed the overall contribution that Kit Carson Electric Cooperative has made to the economic development of northern New Mexico. He stated that the cooperative's Penncro Call Center and Regional Command Center have contributed to employment levels in northern New Mexico and that the cooperative has contributed $15,595,171 in property taxes to Taos, Colfax and Rio Arriba counties. He added that the cooperative has contributed a total of $15,040,296 in county and state taxes during the last five years.

Questions and comments from the committee members addressed:

- the type of propane services provided by the cooperative;
- the cooperative's method of eliminating price spikes in propane during the winter months;
- methods of involving state police officers for dispatch emergency services; and
- whether Kit Carson Electric Cooperative has protested electricity price rate increases.

Recycling Equipment Tax Exemption

English Bird, executive director, New Mexico Recycling Coalition, and Marlene Feuer, director, New Mexico Recycling Coalition, asked the committee members to consider adoption of legislative initiatives to promote recycling in the state. In particular, they advocate a tax credit for the purchase of recycling equipment, including balers, sorting conveyors and glass crushers. The coalition believes that the tax credit could create additional recycling opportunities and increase the amount of material diverted from landfills in New Mexico. Ms. Bird and Ms. Feuer predict that the tax credit would provide an effective incentive to include the business community in recycling efforts. According to the coalition's estimates, 50 percent of waste is generated by commercial entities. Reduction of waste and increased recycling by such entities might, according to the coalition, eliminate much of the state's waste problems.

Questions and comments from the committee members addressed:

- the possibility of the use of recyclable materials in state parks;
- the use and distribution of money in the Tire Recycling Fund;
- whether most tires in the state are recycled;
- whether curbside recycling pickup services exist in various cities; and
- which materials are not cost-effective for recycling purposes.

DWI Affiliate Update

Dr. Tasia Young, legislative liaison, New Mexico Association of Counties (NMAC), Rob Mitchell, chair, and Kevin Kinsey, vice chair, DWI Affiliate, discussed the issue of funding for local DWI programs. They stated that the local DWI grant program funding has decreased by $2.3 million annually over the past two fiscal years as a result of $1.5 million diverted to the Administrative Office of the Courts for drug court programs, $300,000 for ignition interlock indigent funding and an additional $500,000 to the Local Government Division of the Department of Finance and Administration for increased oversight of county DWI programs. The DWI Affiliate takes the position that the Local DWI Grant Fund is not the appropriate funding source for such state programs. The affiliate has found that reduced funding has impacted the ability of county programs to provide local DWI-related services. The affiliate requests an increase in funding for local DWI programs.

Dr. Young, Mr. Mitchell and Mr. Kinsey answered committee member questions from the previous RSTPC meeting in Rio Rancho. They addressed the following: how reductions in services have been realized relative to reduced funding for local DWI programs; specific increased responsibilities that local DWI program coordinators have experienced in the climate of decreased funding; how local program funds are spent; and whether local programs have obtained funding from other sources. Mr. Mitchell and Mr. Kinsey provided the committee members with data regarding the amount of funds provided to individual counties for DWI programs.

Questions and comments from the committee members addressed:

- methods of communicating the success of local DWI programs;
- how unexpended balances in local DWI programs are spent;
- the amount of money in the Local DWI Grant Fund;
- possible monitoring of projected liquor excise tax revenues and communication of those projects to counties for budget adjustment purposes;
- whether poor infrastructure contributes to DWI fatalities;
- the accessibility of local DWI program managers; and
- the results of the Legislative Finance Committee's audit of the Local DWI Grant Fund program.

New Mexico Association of Counties Legislative Priorities

Dr. Young asked the committee for support of the association's legislative priorities for the 2006 legislative session. The NMAC first plans to advocate proposals to reimburse counties for state prisoners housed in county detention facilities. The New Mexico Sentencing Commission and University of New Mexico estimates indicate that the annual cost of housing such prisoners approaches $25 million. Dr. Young indicated that NMAC has requested reimbursement for county prisoner housing costs every year since 1999.

The NMAC also plans to request an increased distribution from the State Fire Fund to local governments. Under current state law, approximately half of the revenues derived from property and vehicle insurance payments is diverted from local fire departments and distributed to the general fund.

Additionally, the NMAC will request assistance to counties for compliance with recent changes in federal and state election laws, such as the federal Help America Vote Act (HAVA) and the new voter identification law approved by the legislature during the 2005 session. Dr. Young stated that recent statutory mandates to report absentee and early voting results by precinct and to create paper ballot trails have created significant additional staffing and equipment costs for county governments. The cost of replacing voting machines to meet the new requirements will affect at least 75 percent of New Mexico's 33 counties and, according to the Office of the Secretary of State, will cost between $14 million and $34 million. The NMAC will seek further legislative action to increase salaries for county-elected officials and to increase term limits for county officials.

Questions and comments from the committee members addressed:

- previous legislative proposals to extend term limits of county officials;
- whether counties have fully implemented the county correctional facility gross receipts tax; and
- whether counties use a portion of the property tax for county correctional facility operations.

Tax Expenditure Budgets

Jim Eads, president and executive director, New Mexico Tax Research Institute, provided the committee with a briefing on tax expenditure budgets. The tax expenditure budget process treats tax incentives and tax subsidies as direct government expenditures for the beneficiaries of those incentives and subsidies. For budget purposes, those tax relief measures are treated in the same manner as direct grants, loans and other forms of government assistance. Ultimately, the tax expenditure budget is intended to provide information that will allow legislative bodies to subject indirect expenditures of public money, including tax incentives and subsidies, to the same degree of scrutiny as direct expenditures of public funds.

Tax expenditures are predominantly measured using three different methods. First, the conceptual baseline approach identifies a benchmark tax base and measures deviations from that base to determine the expenditures that exist in the tax law. The reference low baseline approach measures expenditures based on existing exemptions or exclusions from the tax base. In this approach, some exemptions are not considered as tax expenditures. Under the revenue reducer list approach, revenue reducers are identified as tax exemptions, exclusions or deductions and losses are quantified without reference to any set standard.

Mr. Eads discussed some of the benefits associated with tax expenditure budgets. Some advantages of tax expenditure budgets include their systematic method of identifying and examining the effect of tax breaks and their utility in providing information regarding foregone tax revenues.

Despite the advantages tax expenditure budgets might provide, Mr. Eads noted that they might also create some disadvantages. The expertise and data for initial preparation of such budgets might be costly. In addition, Mr. Eads noted that tax expenditure budgets might become a list of easy elimination targets for certain tax exemptions if the underlying policies that led to the provision of those exemptions are forgotten.

Questions and comments from the committee members addressed:

- the potential value of tax expenditure budgets in identifying unnecessary gross receipts tax deductions; and
- the potential value of tax expenditure budgets in contributing to the understanding of the breadth of the gross receipts tax base.

Tax Credits for Private School Tuition

Troy Williamson, executive director, Educate New Mexico, stated that the mission of Educate New Mexico, a nonprofit organization, is to assist low-income families in paying for private school tuition. Mr. Williamson indicated that Educate New Mexico has assisted 816 children to attend private schools of their parents' choice. This year, 770,000 children have applied with the organization for 430 scholarships.

Educate New Mexico proposes that the legislature provide a tax credit to taxpayers who donate money to nonprofit organizations that provide scholarships to low-income students for private school tuition. Mr. Williamson indicated that similar tax credits exist in Arizona, Florida and Pennsylvania.

Dr. Moises Vengas, executive director, Albuquerque Partnership, expressed support for the legislative action requested by Educate New Mexico. He indicated that such legislation would expand educational options for students who have not performed successfully in the public education system.

Ron Donkersloot, New Mexico Association of Nonpublic Schools, discussed the obstacles that students in nonpublic schools encounter in meeting tuition payments. He indicated that the existence of several nonpublic schools is threatened due to reduced enrollments stemming from high tuition costs. He advocates tax credits for tuition payments and other alternatives to make nonpublic school tuition affordable for families.

Charles Bush, a representative from Chamisa Mesa, a nonpublic school in Taos, stated that nonprofit organizations such as Educate New Mexico have positively affected enrollment at that school. According to Mr. Bush, Educate New Mexico has provided scholarships to six Chamisa Mesa students who would not have attended that school otherwise. Mr. Bush spoke in support of legislation that would grant tax credits for donations to organizations such as Educate New Mexico. He predicts that the number of students at Chamisa Mesa might double if such legislation is enacted.

Questions and comments from the committee members addressed:

- whether private schools provide the best alternative to students struggling in public schools;
- the importance of parental responsibility in improving student performance;
- whether property tax credits should be used to supplement private school tuition programs;
- the potential benefits of providing tax credits to nonprofit organizations that provide private school tuition scholarships;
- private school student transportation needs; and
- the possibility of providing a cap on the amount of tax credits that might be available with respect to legislation advocated by Educate New Mexico.

Hospital Tax Credit

Cindy West and Dan Weaks, New Mexico Hospital Association, and Fred Woody, Carlsbad Medical Center, urged the committee members to consider providing a gross receipts tax credit to for-profit hospitals. Mr. Weaks explained that the gross receipts tax imposed on hospitals in New Mexico contributes to the competitive disadvantages that New Mexico hospitals have relative to out-of-state hospitals and to in-state medical providers that are able to claim existing gross receipts tax deductions for medical services. In addition, New Mexico hospitals often provide a large amount of uncompensated care, which increases their financial burden. To help alleviate such disadvantages, the New Mexico Hospital Association proposes a gross receipts tax deduction for receipts from health care services provided to uninsured patients.

Questions and comments from the committee members addressed:

- the potential fiscal impact of eliminating the gross receipts tax on hospital receipts; and
- the number of patients receiving uncompensated care in New Mexico hospitals.

Friday, September 16

El Prado Water and Sanitation District Requests

John Painter, El Prado Water and Sanitation District, requested that the committee members consider legislation to appropriate funds to the district for capital outlay projects in the district. The district will seek funding for well replacement and to obtain water rights during the 2006 legislative session.

Tax and Expenditure Limits

Bert Waisenen, senior policy specialist, fiscal affairs program, National Conference of State Legislatures (NCSL), summarized a study conducted for the NCSL regarding tax and expenditure limits (TELs). TELs are restrictions on government tax revenues and spending outlays. The study indicated that 23 states have spending limits, four have tax limits and three have both. Many of the TELs were enacted in the late 1970s and early 1990s. Those enactments coincided with economic fluctuations in the United States and, after the property tax revolt in California, the passage of Proposition 13.

Four categories of traditional TELs exist. They include expenditure limits, revenue limits, appropriations limited by revenue estimates and hybrids or combinations. Revenue limits tie allowable yearly increases in revenue to personal income or some other type of index such as inflation or population. The limit provides for the refund of excess revenues to taxpayers. Expenditure limits restrict expenditures with respect to a growth index related to the expansion of the economy. Some expenditure limits contain refund provisions if revenues exceed authorized spending levels. Another TEL restricts appropriations to a percentage of revenue estimates. This variation of a spending limit ties appropriations to revenue forecasts and does not establish an absolute limit or tie growth to a measurable index. Hybrid TELs combine components of various limits. Oregon and Colorado have enacted hybrid TELs.

Mr. Waisenen presented several pros and cons associated with the enactment of TELs. As advantages of enacting TELs, Mr. Waisenen stated that TELs force discipline over budget and tax practices; make government more accountable; and force governments to form creative methods of revenue generation. Some disadvantages of TELs include the shifting of fiscal decision-making away from elected representatives; potential disproportional cuts for nonmandated or general revenue fund programs; and increased difficulty in raising new revenue.

Colorado has received attention from policymakers for its enactment of its Taxpayers' Bill of Rights (TABOR). TABOR is a set of constitutional provisions Colorado voters adopted in 1992 to limit revenue growth for state and local governments and to require that any tax increase by state or local government be approved by the voters of the affected governments. NCSL's study of TELs indicated that Colorado's early experience with TABOR included rapid demographic and economic growth in the 1990s due to substantial migration to the state and the rapid expansion of the electronics and telecommunications industries in the state. Taxpayers received substantial "TABOR refund checks" as revenues were returned to them. The Colorado General Assembly subsequently reduced personal income and sales tax rates to reduce surplus revenues.

In 2000 and 2001, the electronics and telecommunications industries began to decline and Colorado's economy and tax collections were adversely affected. Reduced reserves from those economic changes were exacerbated by the failure of TABOR to permit revenue collections during economic downturns. TABOR prevents the creation of a traditional state rainy day fund through its requirement to refund revenues in excess of specified limits. Reserves of three percent of the general fund are allowed, but any use must be repaid in the following fiscal year. Due to budget problems that have arisen in Colorado, several suggestions to alleviate the impact of TABOR have arisen. Some advocates propose to relax TABOR limits. Other advocates have suggested higher refund base requirements.

Questions and comments from the committee members addressed:

- whether a similar provision in New Mexico would have prevented appropriations of additional oil and gas tax revenues received by the state;
- the cause of the decline of Colorado's electronics and telecommunications industries;
- the amount of Colorado's total budget;
- whether Colorado has any permanent funds; and
- the existence of expenditure limits in New Mexico, to the extent that the legislature cannot appropriate more funds than are generated by the state.

Streamlined Sales and Use Tax Agreement Negotiation Update

Dr. Kelly O'Donnell, assistant secretary and tax policy director, Taxation and Revenue Department (TRD), provided the committee with an update of the TRD's participation with other states in discussing the terms of the streamlined sales and use tax agreement. House Bill 575, which passed during the 2005 legislative session, authorized the secretary of taxation and revenue to enter into multistate negotiations to develop a streamlined sales and use tax agreement if that agreement has specific attributes. That legislation did not, however, commit New Mexico to implementing a streamlined sales tax. Implementation of the terms of the streamlined sales and use tax agreement generally would require destination-based sourcing of the gross receipts tax, uniform gross receipts tax exemption certificates and standardized definitions of terms such as food, drugs, medical equipment, school supplies and computer equipment.

If the terms of the streamlined sales and use tax agreement are implemented in New Mexico, some of the compensating taxpayers might have increased tax burdens. In addition, large cities could lose gross receipts tax revenues to smaller cities where services are ultimately received. However, if the Congress works with streamlined sales and use tax agreement terms to permit states to tax remote sellers, New Mexico would have an additional source of gross receipts tax revenue. Dr. O'Donnell warned that any Congressional action with respect to the taxation of remote sellers is still uncertain.

Adoption of streamlined sales and use tax agreement terms would affect a wide range of statutes affecting New Mexico taxes. First, use of the agreement's definitions would change the meaning of several provisions in New Mexico's tax laws. For instance, the agreement's definition of food differs from the definition of food contained in New Mexico's tax provisions and would affect the provision of tax deductions for gross receipts on food sales. The streamlined sales and use tax agreement's required streamlined exemption certificates would additionally change New Mexico's nontaxable transaction certificate system.

Questions and comments from the committee members addressed:

- a possible study examining the steps necessary to implement the terms of the streamlined sales and use tax agreement;
- the effect of the streamlined sales and use tax agreement upon nonprofit organizations that have obtained tax-exempt status from the Internal Revenue Service;
- the manner in which sales taxes on remote sales would be calculated and tracked throughout the country;
- the necessity for and likelihood of Congressional action on the taxation of remote sales;
- the origin of the streamlined sales and use tax negotiations; and
- the streamlined sales and use tax as a tool to enable the legislature to permit reduced gross receipts tax rates in New Mexico due to increased revenues received from remote sales.

Severance Tax Permanent Fund Distributions

Doug Williams, economist, Legislative Council Service, provided the committee with an overview of how severance tax revenue is distributed. Severance tax revenue is composed of oil and gas severance tax revenues and revenues from the severance taxes on coal and other minerals. Those revenues, which approximated $394 million in fiscal year 2005, were distributed to the Severance Tax Bonding Fund. The money in that fund is used to pay principal and interest on severance tax bonds and on supplemental severance tax bonds. The residual revenues left in the Severance Tax Bonding Fund are then remitted to the Severance Tax Permanent Fund. The balance of the that fund as of June 30, 2005 approximated $3.76 billion. The money contained in that fund is invested in domestic and international equities, private equities, economically targeted investments and core fixed income and high yield bonds. Of the five-year average balance of the Severance Tax Permanent Fund, 4.7 percent is distributed to the general fund. Mr. Williams prepared a table showing the amounts of net severance tax revenues during the last 15 years and the percentages of revenues distributed in the Severance Tax Permanent Fund. The percentages of revenues distributed amounted to 67.8 percent in 1991 and declined to 4.8 percent in 2004.

Questions and comments from the committee members addressed:

- the reduced revenues distributed to the Severance Tax Permanent Fund;
- the necessity to maintain a certain distribution to the Severance Tax Permanent Fund each year; and
- the source of new contributions to the Severance Tax Permanent Fund.

Motor Transportation Division Enforcement Issues

Secretary John Denko, Department of Public Safety (DPS), and Captain Ron Cordova, Motor Transportation Division (MTD) of the DPS, updated the committee on the efforts of the MTD in enforcing certain transportation-related taxes and in dealing with special enforcement issues in the United States-Mexico border region. They noted that due to over 77,000 inspections it conducted last year, the MTD seized more than 30,000 pounds of illegal narcotics with an approximate street value of $40 million.

Secretary Denko and Captain Cordova discussed the MTD's additional enforcement duties with respect to the statutorily required use of weight-distance tax identification permits and the imposition of the trip tax and the caravan tax. Captain Cordova noted that MTD revenues have increased significantly from the previous year due to better enforcement at ports of entry of the fees for oversize and overweight vehicles stemming from the tax identification permit requirements.

Dr. O'Donnell added to the MTD's data regarding improved enforcement of transportation-related taxes. Dr. O'Donnell noted that due to the use of weight-distance identification cards, collections of the trip tax are projected to increase by $2 million to $3 million annually.

Improvement in weight-distance tax collection is also expected. MTD and TRD have shared information pursuant to the federal International Fuels Tax Agreement to identify multistate trucking operators who have not complied with certain taxes. In addition, a new fuels and weight-distance tax processing system will also be ready for implementation by the beginning of fiscal year 2007. That system will enable automated compliance processes. Dr. O'Donnell noted that the program's success will likely improve if funding for two additional weight-distance tax auditors is provided and if certain statutory changes are enacted. The TRD recommends legislation that includes provisions to permit the detainment of vehicles that are not tax compliant; to provide a penalty for failure to stop at a port of entry; to increase penalties for carrying overweight loads and for operating without an oversize or overweight permit; and to provide an additional penalty for failure to carry a weight-distance tax identification card or for failure to carry a log book. If additional auditors and such statutory provisions are provided, Dr. O'Donnell predicts that total weight-distance tax revenue could increase by two percent, or $1.5 million, per year.

Questions and comments from the committee members addressed:

- how often ports of entry are open;
- whether the cost of fuel has affected the use of DPS fleets;
- DPS budget shortfalls in providing for fuel costs;
- accident location identification;
- the source of gasoline for police fleets; and
- the reason for the delay in implementing the weight-distance tax processing system.

The committee adjourned at 3:30 p.m.

Revised: October 19, 2005

TENTATIVE AGENDA
for the
FIFTH MEETING
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

October 20-21
State Capitol, Room 307

<u>Thursday, October 20</u>

8:30 a.m. **Energy, Minerals and Natural Resources Department (EMNRD) Clean Energy Proposals**
—Joanna Prukrop, Secretary, EMNRD
—Craig O'Hare, Special Assistant for Renewable Energy, EMNRD

9:30 a.m. **Laboratory Partnership with Small Business Tax Credit Update**
—Jim Manatt, Focus Energy
—Mike Tripodi, Clean Air Systems
—Vic Chavez, Office of Advocacy and Small Business, Sandia National Laboratories

10:30 a.m. **Consumer Information on Propane Pricing**
—Tony Provencio, President, New Mexico Propane Association

11:30 a.m. **Kit Carson Electric Cooperative Propane Pricing**
—Luis Reyes, Chief Executive Officer, Kit Carson Electric Cooperative
—Andrew Chavez, Propane Division Manager, Kit Carson Electric Cooperative

12:00 noon **Lunch**

1:30 p.m. **New Mexico Municipal League Proposals**
—Bill Fulginiti, Executive Director, New Mexico Municipal League

2:30 p.m. **Sithe Power Plant Update and Proposal**
—Dick Minzner, Lobbyist
—Steve Begaye, Executive Director, Diné Power Authority
—Freddie Sanches, Sithe Global

3:30 p.m. **House Memorial 20 Update**
—Jeff Dye, New Mexico Hospital Association
—Tres Schnell, Department of Health

4:00 p.m. **Telecommunications Access Fund Update**
—Tom Dillon, Executive Director, New Mexico Commission for Deaf and Hard-of-Hearing Persons
—John Hooper, Chief Financial Officer, New Mexico Commission for Deaf and Hard-of-Hearing Persons

4:30 p.m. **Recess**

Friday, October 21

9:00 a.m. **DWI Grant Fund Program Update**
—Joyce Johnson, Local Government Division, Department of Finance and Administration (DFA)
—Dr. Tasia Young, Legislative Liaison, New Mexico Association of Counties

10:00 a.m. **Compensating Tax Structure Study**
—Dr. Kelly O'Donnell, Assistant Secretary and Director of Tax Policy, Taxation and Revenue Department (TRD)

11:00 a.m. **Oil and Gas Revenue Update**
—Dr. Tom Clifford, Chief Economist, TRD

12:00 noon **Lunch**

1:30 p.m. **Taxation of Underground Versus Above Ground Drip Systems**
—John Wortman, Executive Vice President, New Mexico Farm Bureau
—Dr. Mick O'Neill, New Mexico State University (NMSU)
—Dr. Robert Flynn, NMSU

2:30 p.m. **Gross Receipts Tax Deduction for Boxing Promoters**
—Art Jaramillo, Superintendent, Regulation and Licensing Department
—Richard Guay, Athletic Commission, Regulation and Licensing Department

3:30 p.m. **Adjourn**

MINUTES
of the
FIFTH MEETING
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

October 20-21, 2005
State Capitol, Room 307

On October 20, the fifth meeting of the Revenue Stabilization and Tax Policy Committee (RSTPC) for the 2005 interim was held in Room 307 of the State Capitol.

Present

Sen. John Arthur Smith, Chair
Rep. Donald L. Whitaker, Vice Chair
Sen. Ben D. Altamirano
Rep. Janice E. Arnold-Jones
Sen. Carlos R. Cisneros
Sen. Kent L. Cravens (10/21)
Rep. Anna M. Crook
Sen. Joseph A. Fidel (10/20)
Rep. Keith J. Gardner (10/21)
Rep. Roberto "Bobby" J. Gonzales
Rep. Ben Lujan
Rep. Daniel P. Silva
Sen. H. Diane Snyder
Rep. Thomas C. Taylor

Absent

Sen. Mark Boitano
Rep. George J. Hanosh
Sen. William E. Sharer
Sen. James G. Taylor

Designees
Rep. Debbie A. Rodella (*designee for George J. Hanosh*)
Sen. John C. Ryan (*designee for Sen. Mark Boitano on 10/20)*

(Attendance dates are noted for those members not present for the entire meeting.)

Staff
Amy Chavez, Tim Crawford, Cleo Griffith and Pam Ray

Guests
The guest list is in the meeting file.

Thursday, October 20

Call to Order and Approval of Minutes

Senator John Arthur Smith, chair, called the committee to order at 9:40 a.m. The committee unanimously approved the minutes from the fourth meeting of the RSTPC on September 15-16 in Taos.

Energy, Minerals and Natural Resources Department (EMNRD) Clean Energy Proposals

Joanna Prukop, secretary, EMNRD, and Craig O'Hare, special assistant for renewable energy, EMNRD, discussed the activities and benefits of New Mexico clean energy programs. Clean energy initiatives in New Mexico involve the production or use of renewable energy sources, promotion of energy efficiency and use of clean fuels. Mr. O'Hare provided the committee with an overview of solar resources and initiatives in the state, including distributed solar, photovoltaic and solar thermal energy sources. He discussed the potential for projects to develop concentrating solar power in the state and the availability of resources from national laboratories to develop this technology. He also discussed the potential for development of biomass and wind-power technologies in the state.

Energy efficiency initiatives are an additional priority of EMNRD. Mr. O'Hare explained that the development of energy-efficient technologies is essential in reducing high gasoline and natural gas costs. EMNRD supports initiatives to build highly energy efficient buildings, also known as green buildings. Green building techniques are encouraged in the construction of public buildings such as schools.

Mr. O'Hare provided the committee with an overview of the benefits of clean energy programs. Among those benefits are the positioning of the state as a leader in the emerging clean energy economy and the reduction of consumer energy bills. Additional benefits include reduction of state operating costs, the protection of New Mexico's natural areas, reduction of consumptive water use and reduction of air pollution and greenhouse gas emissions.

Secretary Prukop described various clean energy programs in New Mexico. The 2005 Efficient Use of Energy Act created one of those programs. The act requires electric and gas utilities to develop energy efficiency programs, which must be deemed cost effective to be approved by the Public Regulation Commission. The Clean Energy Grants Program, created in 2003, provides funding for clean energy projects for public schools, local governments and tribal entities.

The department plans to support several clean energy proposals during the 2006 legislative session. The proposals will include distributed solar tax incentives, amendments to the Renewable Energy Production Tax Credit and gross receipts tax exemptions for concentrating solar power projects. Funding for clean energy grants will also be sought during the upcoming legislative session.

Questions and comments from the committee members addressed:

- the reason for slower growth in the photovoltaic sector in New Mexico relative to other states;
- safeguards that might be employed to encourage only companies with adequate

technologies and workforces to develop clean energy technologies;
- the efforts of EMNRD in changing building codes to promote energy efficiency;
- which states are candidates for development of concentrating solar power projects;
- the resources that New Mexico has to offer in development of concentrating solar power projects;
- the effectiveness of tax credits alone in the promotion of growth in the solar energy market;
- whether the development of fusion as a power source is prevalent;
- large land areas that might be needed for the development of wind power;
- participation of universities in promotion of energy efficiency projects; and
- the percentage of clean energy produced in New Mexico.

Laboratory Partnership with Small Business Tax Credit Update

Victor Chavez, Office of Advocacy and Small Business, Sandia National Laboratories (SNL), asked the committee members to support additional tax credits pursuant to the Laboratory Partnership with Small Business Tax Credit Act. The act provides tax incentives to national laboratories to promote small business development through the use of laboratory resources. Tax credits provided to SNL have assisted SNL in expanding its New Mexico Small Business Initiative to address small business needs and requirements with expertise and resources from the laboratories. Mr. Chavez encouraged committee members to consider providing additional tax credits to promote continued growth of the program. He introduced Jim Manatt of Focus Energy Corporation and Dr. Mike Tripodi of Clean Air Systems, who discussed how their start-up businesses have benefited from the use of SNL resources. Mr. Manatt and Dr. Tripodi also provided committee members with an overview of the activities and goals of their respective companies. Focus Energy Corporation develops technologies to facilitate oil field development, while Clean Air Systems develops technologies to reduce particulate matter, carbon monoxide and hydrocarbon emissions from diesel engines.

Questions and comments from the committee members addressed:
- whether technologies developed by Focus Energy Corporation are being used;
- whether technologies developed by Focus Energy Corporation might be used to find natural resources such as water;
- the manner in which SNL's New Mexico Small Business Initiative evaluates small business candidates that receive SNL assistance; and
- the potential return on investment to the state in discovering untapped oil resources using technologies such as those developed by the Focus Energy Corporation.

Consumer Information on Propane Pricing

Tony Provencio, president, New Mexico Propane Gas Association (NMPGA), provided the committee with an overview of the propane industry's role in informing consumers about energy costs. According to Mr. Provencio, the price of propane is influenced by several factors, including crude oil and natural gas prices, supply and demand and weather conditions. Mr. Provencio mentioned that propane is distributed by 136 propane marketer locations throughout the state. Mr. Provencio discussed factors that have driven propane prices up, including recent natural disasters. In response to propane price spikes, the propane industry placed radio advertisements to encourage propane consumers to contact propane dealers to discuss methods to reduce propane price volatility. As a result of the passage of Senate Memorial 1 during the last special session, the propane industry is also providing information to customers about the state's Low-Income Home Energy Assistance Program. In addition, the NMPGA plans to begin a new initiative to pay $300 of the cost to replace inefficient electric water heaters with more cost-effective water heaters in homes. The NMPGA estimates that the new propane water heaters will save New Mexico consumers an estimated $25,000 each year, or a total of $275,000 over the eleven-year estimated life of the water heaters.

Mr. Provencio discussed the cost of liability insurance for propane marketers. He stated that the hazardous nature of propane distribution has made propane marketers a prime target for lawsuits involving property damage and personal injury. Although the NMPGA believes that propane marketers should be held responsible for incidents in which they are at fault, the association also holds that the marketer should not be held liable when the marketer had no role in the cause of an accident. The association thus will seek support from legislative members during the upcoming legislative session for statutory protection from lawsuits involving accidents not caused by the propane industry. Mr. Provencio stated that such legislation might ultimately reduce insurance costs and energy prices for consumers.

Questions and comments from the committee members addressed:
- the expected increase in propane prices;
- regional propane price estimates;
- whether the propane industry is regulated by the Public Regulation Commission;
- average propane costs for consumers;
- employment in the propane industry;
- the purchase of propane on credit; and
- propane company actions in the event of consumer payment default.

Kit Carson Electric Cooperative Propane Pricing

Andrew Chavez, propane division manager, Kit Carson Electric Cooperative, discussed the propane pricing strategies that the cooperative employs to provide affordable prices to consumers in the wake of increasing fuel costs. The cooperative sets a fixed price per gallon of propane. The cooperative has used financial tools and bulk storage capacities to stabilize prices for customers during the last five heating seasons. Despite the cooperative's efforts, high fuel costs have caused the cooperative to increase prices per gallon of propane. However, Mr. Chavez stated that the cooperative continues to offer fixed and affordable prices to customers. He indicated that fixed prices assist customers in avoiding unpredictable heating costs during the winter months. In addition to fixed prices, the cooperative offers budget billing to permit customers to spread heating costs over a twelve-month period. The cooperative also works with low-income heating programs such as the Low-Income Home Energy Assistance Program, Open Hands, Self Help and the Home Education Livelihood Program.

Questions and comments from the committee members addressed:
- whether Kit Carson Electric Cooperative can participate with the New Mexico Propane Gas Association with respect to safety issues;
- whether the cooperative has adopted a policy to prevent heating shutoffs in the winter months;
- propane industry competitors;
- consumer heating shutoff device availability;

- whether the cooperative's propane division is a for-profit entity; and
- the manner in which the cooperative recovers from deficiencies that arise from charging fixed prices during the winter months.

New Mexico Municipal League Proposals

Bill Fulginiti, executive director, New Mexico Municipal League (NMML), indicated that on October 1, 2005, the NMML board of directors adopted its legislative priorities for the 2006 legislative session. The NMML adopted four tax proposals. Legislation that will be supported by the NMML during the upcoming session will include separate proposals to:

- provide authority to local governments to impose a local option gross receipts tax;
- swap a distribution of the municipal gross receipts tax for a distribution of personal income tax that would be returned to the site of residence;
- permit municipalities to enact a low-income property tax rebate program; and
- permit tax increment financing of local projects.

The NMML will also seek support from the legislature for proposals to improve safety and law enforcement and to fund local libraries; street, road and bridge projects; emergency service personnel initiatives; and regional transit districts.

Questions and comments from the committee members addressed:

- the percentage of the state gross receipts tax that municipalities receive;
- the manner in which municipalities are coping with high energy costs;
- whether trading gross receipts tax for income tax distributions will affect tax burdens on in-state residents more than out-of-state consumers;
- the administration of a potential local option compensating tax;
- whether the highway projects contained in Governor Richardson's Investment Partnership, which passed in 2003, are fully funded;
- capital outlay revenues received by municipalities and unexpended balances; and
- who enforces outstanding capital outlay balance spending.

Sithe Power Plant Update and Proposal

Steve Begaye, executive director, Dineh Power Authority, Richard Minzner, lobbyist, and Freddie Sanches, Sithe Global Power, LLC, provided the committee with an update of efforts with respect to the Desert Rock Energy Project. The project involves the development, financing, construction and operation of a coal-fired electric generating facility at the proposed site on Navajo Nation land near Farmington. During the course of the project's operation and construction, gross receipts taxes and compensating taxes attributable to the project would be payable to the state. The Dineh Power Authority is concerned that the combined state and tribal taxes have raised cost concerns with respect to construction of the plant. Mr. Minzner indicated that the Navajo Nation is willing to reduce the tax burden imposed on the project if the state makes a similar tax concession. According to Mr. Minzner, $60 million in compensating taxes and an additional $320 million are expected to be generated in gross receipts taxes during the project's construction and operation beginning in 2006 and ending in 2033. Mr. Minzner proposed that the legislature allow the state to forgo 15 percent of those revenues through gross receipts tax and compensating tax deductions.

Questions and comments from the committee members addressed:

- the ownership of the coal generating facility;
- the consumers of the power generated by the plant; and
- whether wholesale power sales would be exempt from the gross receipts tax.

House Memorial 20 Update

Jeff Dye, co-chair of the Targeted-Issue Trauma System Committee created by 2005 House Memorial 20, discussed the mission and findings of the committee. That committee was created to study and improve the statewide system of trauma care in New Mexico. Mr. Dye provided several trauma statistics. According to Mr. Dye, New Mexico's trauma death rates are 66 percent higher than national death rates. New Mexico leads the nation in pedestrian deaths and unintentional deaths and is tied for first in violent death rates. Alcohol is involved in 44 percent of motor vehicle crashes, 75 percent of pedestrian crashes, 76 percent of assaults, 66 percent of penetrating injuries and 25 percent of all other injuries.

Mr. Dye indicated that New Mexico is experiencing a crisis in providing adequate trauma care. Despite the high number of trauma-related injuries in the state, New Mexico has only three hospitals designated as trauma centers. Many areas of the state have inadequate access to trauma care. Patients must often, therefore, experience long waits, delayed treatment and unavailable beds. According to Mr. Dye, New Mexico should have 35 neurosurgeons, but has fewer than 10. Moreover, due to treatment of a large number of patients without the ability to pay, trauma care providers have experienced financial difficulties. In 2004, the overall loss on trauma care for New Mexico's trauma centers was estimated at 26 percent of costs, or about $19.3 million.

As a result of its study, the Targeted-Issue Trauma System Committee developed recommendations to provide funding to strengthen existing trauma centers and encourage the construction and operation of new trauma centers throughout the state. Some proposed funding methods include diverting funds from the alcohol excise tax, the automobile insurance premium tax, the Tobacco Settlement Program Fund, the General Fund surplus or the Severance Tax Bonding Fund. The committee also suggests providing funds to enhance Medicaid matching funds for trauma system enhancement.

Questions and comments from the committee members addressed:

- the manner in which reported statistics are gathered;
- whether funding will be used primarily for services or for capital costs;
- whether trauma centers can use county indigent funding to alleviate some costs; and
- the recommended trauma center resources for new centers.

Telecommunications Access Fund Update

Thomas Dillon, executive director, New Mexico Commission for Deaf and Hard-of-Hearing Persons, provided the committee with an update of the status of the Telecommunications Access Fund. Money in the fund consists of revenues derived from a telecommunications relay service surcharge imposed for the use of intrastate telephone and communications services. Fund revenues are used to provide telecommunications access to hearing- or speech-impaired New Mexicans who are unable to use traditional telecommunications equipment without assistance. Mr. Dillon stated that the fund has grown due to increased cell phone and landline use. However, the expansion of Voice Over Internet Protocol (VOIP) might later threaten the use of those methods of communication and could likewise threaten the revenue stream of the fund. Committee members expressed concern about the potential threat that VOIP may pose to traditional means of telecommunications.

Friday, October 21

DWI Program Fund Update

Joyce Johnson, Local Government Division, Department of Finance and Administration, Dr. Tasia Young, legislative liaison, New Mexico Association of Counties, and Rob Mitchell, DWI grant program administrator provided the committee with a report of funds received by each county through the DWI Program Fund. The report included budget reports for each county, which contained budgeted amounts for different types of DWI enforcement, treatment and prevention programs.

Questions and comments from the committee members addressed:

- methods of program effectiveness evaluation;
- the need to let communities drive the budgeting needs for local DWI programs;
- whether unexpended balances in local DWI fund reserves are carried over;
- the number of community members that have benefited from local DWI programs;
- the levels of funding by localities for local DWI programs;
- appointment of the statewide DWI grant council; and
- the merit of addressing alcoholism problems before targeting DWI issues.

Compensating Tax Structure Study

Senate Joint Memorial 46, passed during the 2005 legislative session, requested the Taxation and Revenue Department (TRD) to study the potential competitive disadvantages to in-state businesses inherent in New Mexico's gross receipts and compensating tax structure. The TRD conducted the study and provided the RSTPC members with a report of its findings.

Dr. Tom Clifford, chief economist, TRD, first explained how the compensating tax is imposed in New Mexico. The tax is generally imposed for the use of property acquired outside of the state, and that would have been subject to the gross receipts tax. Dr. Clifford indicated that during fiscal year 2005, the TRD collected $54.2 million in compensating taxes. Of that amount, 80 percent was distributed to the General Fund and 10 percent was distributed to the Small Cities Assistance Fund. The remaining 10 percent was distributed to the Small Counties Assistance Fund.

Dr. Clifford provided the committee with information regarding the payment of the compensating tax by businesses in different industry sectors. Of the industries for which data was collected, the health services industry paid the least amount in compensating tax, while utilities paid the most.

The TRD study identified three major anticompetitive effects caused by the compensating tax structure. First, the tax does not apply to services or intangible property. Thus, consumers have an incentive to purchase out-of-state goods and intangible property. Second, there are no local option tax rates. Since the compensating tax rate of five percent is ultimately lower than the five percent gross receipts tax rate and the added local option gross receipts tax rates, consumers have another incentive to purchase out-of-state goods and services.

Finally, state law prohibits the collection of the compensating tax with respect to the purchase of household items. Thus, if household consumers purchase goods such as furniture from out-of-state sellers, the consumers pay only the out-of-state sales tax and are not responsible for any compensating tax for the purchase. Consumers might thus ultimately choose to purchase goods from states with sales tax rates that are lower than the New Mexico gross receipts tax rate.

Dr. Clifford indicated that at least four solutions to the competitive disadvantages of the compensating tax structure might exist. First, the legislature might impose the compensating tax on services and repeal the gross receipts tax exemption for certain services performed outside of the state. That action might eliminate the tax advantage to consumers of purchasing services from out-of-state sellers. However, Dr. Clifford warned that since most sales of services are between businesses, the added taxes might contribute to tax pyramiding.

Another solution includes the elimination of the prohibition of compensating tax imposition on residential purchases. New Mexico could follow the practice of most states with sales and use taxes and require households to report their taxable purchases on their personal income tax returns. This solution would likely eliminate the tax advantage from out-of-state sellers. On the other hand, additional recordkeeping requirements for households and only small revenue gains might act as a disincentive to enforce the compensating tax on residential households.

Imposition of a local option compensating tax might additionally alleviate the problems inherent in the existing compensating tax structure. A local option compensating tax could be imposed in the same manner as a local option gross receipts tax. The local option tax could also eliminate the tax advantage of buying from out-of-state sellers by ensuring greater tax rate parity with other states. Administrative costs generated by the tax, however, might be significant.

Finally, Dr. Clifford indicated that New Mexico's conformance with the Streamlined Sales and Use Tax Agreement might serve as an effective alternative in improving the state's compensating tax structure. By becoming an agreement participant, the state could join other states in taxing remote sellers that do not have any business presence in the state. This ability would be dependent on congressional action. Since there are many solutions to the compensating tax structure problems and because of uncertain potential for the Streamlined Sales and Use Tax Agreement to provide solutions, the TRD recommends that it should report to the RSTPC in 2006 the advantages and disadvantages of conforming with the Streamlined Sales and Use Tax Agreement.

Questions and comments from the committee members addressed:

- the actions taken by TRD to simplify business tax reporting requirements;
- the percentage of Internet purchases made by households;
- whether the Streamlined Sales and Use Tax Agreement will affect alcohol and cigarette sales;
- whether Congress will enact legislation to permit states to tax remote sales; and
- whether the Streamlined Sales and Use Tax Agreement terms are consistent with a national retail sales tax.

Oil and Natural Gas Industry Update and Outlook

Dr. Tom Clifford, TRD, discussed the supply and demand factors that affect oil and natural gas prices and revenues in New Mexico. Dr. Clifford indicated that natural gas sales have declined by about 5 percent since 2001. Production has stabilized to approximately 1,560 billion cubic feet during the last two years. The average New Mexico price increased by 22 percent in fiscal year 2005 from the 2002 average price. In fiscal year 2005, gross natural gas industry revenue was approximately $9 billion, which is about double the historical norm. The price increases were significantly driven by the natural disasters of 2005. Despite the fact that recent disasters have driven Henry Hub prices, western natural gas prices have not been as affected.

Oil production has decreased during the last two years. The annual average oil price has correspondingly increased by 39 percent in fiscal year in 2005, a cumulative increase of almost 100 percent since 2002. Oil industry revenue was approximately $2.8 billion, about double the historical average. Oil price increases began in fiscal year 2005 before Hurricane Katrina occurred. Those increases indicated strong demand pull and a tight global supply margin. Despite waning supply levels, drilling activity in North America is at an all-time high. New Mexico drilling is also at a high of 79 rigs.

Dr. Clifford provided the committee members with an overview of the natural gas and oil markets. He stated that hurricane-related production outages will result in low natural gas inventories at the beginning of the heating season. Those inventories might improve significantly by next winter if the hurricane season improves; if imports of liquefied natural gas increase; if domestic production increases; and if industrial demand growth is reduced.

With respect to the oil market, hurricane-related disruptions have escalated prices over already high levels due to demand growth and tight supply margins. Long-term factors that might affect the oil market in the future include political stability in oil-exporting regions and the emergence of China and India in the world oil market. Short-term factors include record worldwide drilling activity and shortages in new oil supply sources. Oil and gas production state and local revenues are projected to be approximately $1.748 billion in fiscal year 2006; $1.660 billion in fiscal year 2007; $1.509 billion in fiscal year 2008 and $1.358 billion in fiscal year 2009.

Questions and comments from the committee members addressed:

- the reason for production reductions despite increased rig purchases;
- whether increased gross receipts tax revenues are generated from higher natural gas prices;
- gas price differentials in different localities;
- the effect of increased regulatory requirements on in-state drilling; and
- gasoline consumption levels.

Taxation of Irrigation Systems

Dr. Mick O'Neill, New Mexico State University (NMSU), and Dr. Robert Flynn, NMSU, discussed the benefits of using underground drip irrigation systems for farming purposes. Dr. Flynn indicated that underground drip irrigation systems are often more efficient than above-ground drip systems. Despite the benefits of the increased efficiency of underground systems, gross receipts taxes imposed on the sale of those systems are higher than those imposed on the sale of above-ground systems. The sale of the components of above-ground systems are subject to a 50 percent gross receipts tax deduction pursuant to Section 7-9-62 NMSA 1978 for the sale of agricultural implements to farmers or ranchers. According to written testimony submitted, the difference in tax treatment stems from TRD regulation requirements. Hoyt Pattison, lobbyist, Dairy Producers of New Mexico, encouraged committee members to support legislation to permit gross receipts tax exemptions for the sale of underground drip irrigation systems.

Questions and comments from the committee members addressed:
- the need to encourage greater crop yields;
- whether assistance is available to farmers in making transitions to underground drip irrigation methods; and
- whether the TRD might change regulatory barriers to permit gross receipts tax deductions for the sale of underground drip systems.

Gross Receipts Tax Deduction for Boxing Promoters

Art Jaramillo, superintendent, Regulation and Licensing Department (RLD), Richard Guay, Athletic Commission, RLD, and Dennis Lada, executive director, New Mexico Sports Authority, asked the committee to support legislation to exempt boxing promoters from the gross receipts tax. Superintendent Jaramillo indicated that New Mexico is not competitive in attracting boxing promoters and boxing events to the state. T.J. Trujillo, a New Mexico boxing promoter, added that boxers also are not attracted to pursue their boxing goals in New Mexico because of the low-paying events sponsored in the state.

Questions and comments from the committee members addressed:
- the number of in-state boxing promoters and fighters;
- whether it is the state's responsibility to provide a market for boxing events;
- whether a boxing commission is needed to regulate boxing standards in New Mexico;
- whether boxing events would be more successful than concert events; and
- whether the state could develop professional wrestling.

The committee adjourned at 4:30 p.m.

Revised: November 29, 2005

TENTATIVE AGENDA
for the
SIXTH MEETING
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

November 30
Room 307, State Capitol

December 1
Room 322, State Capitol

<u>Wednesday, November 30</u>

8:00 a.m. **Call to Order**

8:05 a.m. **Approval of Minutes**

8:10 a.m. **Daily Bed Surcharge**
—Carolyn Ingram, Human Services Department (HSD)

9:10 a.m. **Gross Receipts Tax Elimination on Medical Service Providers**
—Carolyn Ingram, HSD
—Randy Marshall, New Mexico Medical Association

9:45 a.m. **Economic Development Incentives**
—John Tull, Deputy Secretary, Economic Development Department

10:15 a.m. **Food Tax Update**
—Dr. Kelly O'Donnell, Assistant Secretary and Director of Tax Policy, Taxation and Revenue Department (TRD)

10:45 a.m. **Personal Income Tax Rate Reductions**
—Dr. Kelly O'Donnell, TRD

11:00 a.m. **Gross Receipts Tax Pyramiding Options**
—Jim Eads, President and Executive Director, New Mexico Tax Research Institute (NMTRI)
—Dr. Manuel Del Valle, Research Director, NMTRI

11:30 a.m. **Tax Increment Financing**
—Raymond Sanchez
—Robert Desiderio
—Mike Daley

12:30 p.m. **Break**

12:45 p.m. **Educational Retirement Fund Update**
—Evalynne Hunemuller, Director, Educational Retirement Board
—Greg Geisler, Legislative Finance Committee

1:30 p.m. **General Fund Revenue Update**
—Jan Goodwin, Secretary, TRD
—James Jimenez, Secretary, Department of Finance and Administration
—David Abbey, Director, Legislative Finance Committee

3:00 p.m. **Proposed Legislation Discussion and Adoption**

Alcohol Purchase Electronic Age Verification
—Senator Kent L. Cravens, Member, Revenue Stabilization and Tax Policy Committee

3:30 p.m. **Sithe Global and Dine Power Authority Proposal**
—Richard Minzner, Lobbyist
—Freddy Sanches, Vice President, Sithe Global, L.L.C.
—Steve Begaye, General Manager, Dine Power Authority

4:00 p.m. **Gross Receipts Tax Deduction for Hospital Construction**
—Representative Jose A. Campos

4:30 p.m. **Biomass Gross Receipts Tax Deduction**
—Representative Hector H. Balderas
—Art Hull, Public Service Company of New Mexico

5:00 p.m. **Recess**

Thursday, December 1

8:30 a.m. **Proposed Legislation Discussion and Adoption**

Hospital Gross Receipts Tax Deduction
—Cindy West, Lobbyist, New Mexico For-Profit Hospitals
—Dan Weaks, New Mexico Hospital Association

9:00 a.m. **Deduction for Medical Service Providers**

9:30 a.m. **Chemical Gross Receipts Tax Deduction**
—Dan Najjar, Lobbyist

10:00 a.m. **Underground Irrigation Systems Deduction**

10:30 a.m. **Recycling Tax Incentives**
—Joseph Ellis, President, New Mexico Recycling Coalition (NMRC)
—English Bird, Executive Director, NMRC

11:00 a.m. **Tax Credit for Private Schools**

11:30 a.m. **Energy, Minerals and Natural Resources Department (EMNRD) Clean Energy Proposals**
—Joanna Prukrop, Secretary, EMNRD
—Craig O'Hare, Director of Renewable Energy, EMNRD

12:00 noon **Lunch**

1:30 p.m. **Taxation and Revenue Department Proposals**
—Dr. Kelly O'Donnell, TRD

3:30 p.m. **New Mexico Municipal League Proposals**
—Bill Fulginiti, New Mexico Municipal League

4:30 p.m. **Gross Receipts Tax Deduction for Professional Contests**
—Arturo Jaramillo, Superintendent, Regulation and Licensing Department

5:00 p.m. **Adjourn**

MINUTES
of the
SIXTH MEETING
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

November 30
Room 307, State Capitol

December 1
Room 322, State Capitol

The sixth meeting of the Revenue Stabilization and Tax Policy Committee (RSTPC) for the 2005 interim was called to order by Senator John Arthur Smith, chair, on Wednesday, November 30, at 8:25 a.m. at the State Capitol.

Present
Sen. John Arthur Smith, chair
Sen. Ben D. Altamirano
Rep. Janice E. Arnold-Jones
Sen. Mark Boitano (12/1)
Sen. Carlos R. Cisneros (11/30)
Sen. Kent L. Cravens (11/30)
Rep. Anna M. Crook
Rep. Roberto "Bobby" J. Gonzales
Rep. George J. Hanosh
Rep. Ben Lujan
Sen. William E. Sharer (11/30)
Rep. Daniel P. Silva
Sen. H. Diane Snyder (12/1)
Sen. James G. Taylor
Rep. Thomas C. Taylor

Absent
Rep. Donald L. Whitaker, vice chair
Sen. Joseph A. Fidel
Rep. Keith J. Gardner

Designees
Rep. William "Ed" Boykin (*designee for Rep. Keith J. Gardner*)
Sen. Nancy Rodriguez (*designee for Sen. Joseph A. Fidel*)
Rep. Henry Kiki Saavedra (*designee for Rep. Donald L. Whitaker*)

(Attendance dates are noted for those members not present for the entire meeting.)

Staff
Amy Chavez, Cleo Griffith, Pam Ray and Tim Crawford

Guests
The guest list is in the meeting file.

Wednesday, November 30

Call to Order

Senator Smith called the meeting to order at 8:25 a.m.

Daily Bed Surcharge

Carolyn Ingram, Human Services Department (HSD), provided the committee with a description of legislation that resulted in the imposition of the daily bed surcharge, more commonly known as the bed tax. The surcharge became law as the result of the passage of Senate Bill 385 during the 2004 legislative session. The surcharge of $8.25 per occupied bed per day is imposed on licensed nursing homes, licensed intermediate care facilities for the mentally retarded and licensed residential treatment centers. Some proponents of the surcharge hoped to generate federal matching funds for the Medicaid program.

To offset the increased costs to non-Medicaid patients or their families resulting from the daily bed surcharge, the legislature also passed separate legislation in 2004 to create an income tax credit for expenses paid to licensed nursing homes, licensed intermediate care facilities for the mentally retarded and licensed residential treatment centers. After the legislation passed, the federal Centers for Medicare and Medicaid Services (CMS) of the Social Security Administration expressed concern that the daily bed surcharge constituted a provider tax in violation of the Social Security Act and that federal matching funds could not be provided to the state so long as a credit to offset the daily bed surcharge remained in effect. To respond to federal concerns, the legislature repealed the tax credit in 2005. The CMS, however, ruled that revenues raised by the state from the daily bed surcharge while the tax credit was in effect could not be matched by the federal government for the Medicaid program due to what it deemed as a violation of the Social Security Act. The HSD has appealed the decision of the CMS. Ms. Ingram indicated that states with similar cases, including Hawaii, Louisiana and Tennessee, have filed successful administrative appeals and are currently negotiating settlements with the CMS. Meanwhile, the funds generated by the daily bed surcharge during the period of the tax credit's effectiveness have been set aside until a conclusion on the HSD's appeal is reached.

Ms. Ingram indicated that the Medical Assistance Division of the HSD has considered different options in determining how to best obtain funding for Medicaid and in determining the role of the daily bed surcharge in raising funds. Those options will be presented to the Legislative Finance Committee (LFC) before the end of 2005. Ms. Ingram estimated that a repeal of the daily bed surcharge might result in a $20 million loss to the state.

Questions and comments from the committee members addressed:

- the fiscal impact of repealing the income tax credit for expenses paid to licensed nursing homes, licensed intermediate care facilities for the mentally retarded and licensed residential treatment centers;
- whether urgency to fund Medicaid programs still exists;
- the policy implications of repealing the income tax credit for nursing home facility expenses;
- whether fees for certain types of physicians might be raised to obtain revenues;
- the amount of money that the state might lose as the result of a lost appeal;

- whether nursing homes obtained indirect benefits from the imposition of the daily bed surcharge; and
- whether New Mexico should reinstate the income tax credit if it wins its appeal against the CMS.

Gross Receipts Tax Elimination on Health Care Practitioners

Ms. Ingram and Randy Marshall, director, New Mexico Medical Association, discussed the effects of legislation that passed in 2004 to provide for a deduction from gross receipts for the receipts of health care practitioners. That deduction applies to receipts from payments by managed health care providers or health care insurers for commercial contract services or Medicare Part C services provided by health care practitioners. Fee-for-service payments are not deductible. Mr. Marshall warned that although elimination of the gross receipts tax has a positive effect upon recruiting physicians to practice in New Mexico, narrowing the tax base excessively might result in a CMS ruling that the gross receipts tax on physicians constitutes a provider tax. He also discussed physician efforts to receive a greater reimbursement rate from managed care programs in New Mexico. Mr. Marshall further discussed state efforts to recruit physicians to rural areas of the state.

Questions and comments from the committee members addressed:

- the possibility of including other classes of physicians, such as chiropractors, as among the eligible for the gross receipts tax deduction for health care practitioners;
- the burdens imposed upon taxpayers for the double local option penalty for misreporting the gross receipts tax deduction for health care practitioners;
- whether the physician retention rate in New Mexico has risen;
- the distribution of physicians throughout the state;
- programs that might encourage students educated in rural areas to obtain medical degrees and practice in those rural areas; and
- the number of temporary medical physicians practicing in-state.

Update on Food and Medical Gross Receipts Tax Deductions

Dr. Kelly O'Donnell, assistant secretary and tax policy director, Taxation and Revenue Department (TRD), provided the committee with an update of gross receipts tax deductions reported by food retailers and health care practitioners for the sales of food and services provided by health care practitioners. According to Dr. O'Donnell, the total deductions averaged $232 million per month in the first nine months. Deductions for the sale of food averaged $187 million per month, while deductions for health care practitioner services averaged $44 million per month. Consumers realized cost savings of approximately $14.5 million per month on purchases of food and medical care as a result of the deductions for retailers and health care practitioners.

The TRD estimates that as a result of the food and health care practitioner gross receipts tax deductions, general fund collections decreased by $7.8 million per month. However, general fund collections increased by $11.9 million per month due to a repeal of a .5 percent credit to municipalities. Hold harmless distributions to local governments averaged $7.2 million. Overall, net general fund revenue decreased by $3.1 million per month.

Questions and comments from the committee members addressed:

- whether the TRD has explored alternatives to imposing a double local option penalty for misreporting the food and health care practitioner deductions; and
- whether the imposition of additional local option taxes might affect hold harmless distributions to municipalities.

Economic Development Incentives

John Tull, deputy secretary, Economic Development Department (EDD), discussed the progress of various tax incentives in retaining and attracting companies to the state and in contributing to the state's economic growth. Mr. Tull indicated that New Mexico ranks as twelfth in the nation in job growth and is outpacing the nation in personal income growth. Mr. Tull stated that there are currently 27 tax incentives in state law. Programs such as the Job Training Incentive Program, Film Workforce Training Program and Film Mentorship Program are counted by the EDD as additional incentives for economic development. Mr. Tull stated that 20 percent of the tax incentives provided by the state are used 80 percent of the time. Those incentives include the rural jobs tax credit, the high wage jobs tax credit, the investment tax credit, the job training incentive program, the film production rebate, the child care tax credit and tax incentives associated with industrial revenue bonds. Specialized incentives are also used to target specific industries, such as aircraft and hi-tech industries. The EDD attributes the attraction of companies such as Monarch Litho, Southwest Cheese, Kendal Precision Machining and Ktech to the provision of state tax incentives. Mr. Tull indicated that the EDD will continue to aggressively promote tax incentives to expand New Mexico businesses and to recruit new business to the state.

During the 2005 legislative session, House Joint Memorial 11 was introduced. The memorial requested the EDD and TRD to survey the best practices of other states and to study methods through which economic development information and data tied to tax incentives should be collected. The memorial requested that the departments recommend methods for analyzing the information and data and estimating economic impacts of tax incentives. Although the memorial did not pass, the EDD, TRD, Department of Finance and Administration (DFA), Labor Department, LFC and private sector economic development and business professionals formed a task force to make such determinations. Mr. Tull stated that the task force is currently working to reach a consensus on the recommendations that it will bring to the legislature for the 2006 legislative session.

Questions and comments from the committee members addressed:

- companies attracted to the state versus those that are expanding in the state;
- whether the Job Training Incentive Program has effectively produced new jobs;
- the impact that the Job Training Incentive Program has made in training Intel employees;
- whether employees trained pursuant to the Job Training Incentive Program use the skills learned through training for the same employers that trained them;
- the potential utility to permanent legislative committees of the findings of the task force;
- whether any employment opportunities exist for seasonal employees; and
- the need to provide sufficient training in schools to attract new industries.

Personal Income Tax Rate Reductions

Dr. O'Donnell provided the committee with an overview of changes to the personal income tax rates that were enacted during the 2005 regular session and the 2005 special session. During the 2005 regular session, changes in the top personal income tax rate, which were scheduled to decrease from 6 percent in 2005 to 5.3 percent in 2006 and to 4.9 percent in 2007 and in subsequent years, were delayed. As a result, the legislation changed the top rate from 5.3 percent to 5.8 percent in 2006 and from 4.9 percent to 5.3 percent in 2007. The rate under the 2005 regular session legislation would not have changed the 2008 rate.

The top personal income tax rates were again changed during the 2005 special session. The top personal income tax rate during the 2005 tax year was reduced from 6 percent to 5.7 percent. The top rate for 2006 was reduced from 5.8 percent to 5.3 percent. The 5.3 percent rate for 2007 and for subsequent years enacted during the regular session remained the same.

According to the TRD, reducing the 2006 top personal income tax rate to 4.9 percent would result in reduced state revenues of $25.4 million in fiscal year 2006, $58.5 million in fiscal year 2007 and $33.3 million in fiscal year 2008.

Gross Receipts Tax Pyramiding Options

Jim Eads, president and executive director, New Mexico Tax Research Institute (NMTRI), and Dr. Manuel Del Valle, research director, NMTRI, provided the committee with a report of pyramiding transaction taxes in New Mexico. Mr. Eads explained that as the sales of services become a greater portion of New Mexico's economy, pyramiding effects might be exacerbated as determination of the location of the sale and as definition of inputs becomes increasingly complicated. Mr. Eads cited a recent study that identified New Mexico as among the states with the highest incidence of taxed services. However, Mr. Eads stated that pyramiding is not unique to New Mexico and that any state that imposes a sales-type tax will create some pyramiding. He also warned that New Mexico's broad tax base is in compliance with a basic principle of tax policy that encourages broad tax bases. He stated that although some relief might be necessary to reduce the negative impact of pyramiding in New Mexico, that relief should not eviscerate the gross receipts tax system that has been successful for the state.

In response to the committee's request, Mr. Eads identified possible options for gross receipts tax pyramiding reduction. First, relief might be given to industries most impacted by pyramiding by offering those industries tax relief. Relief might also be given to businesses that purchase goods and services that are taxed in New Mexico but not in other states. Finally, relief might be granted to all businesses predicated on the taxability of goods and services in New Mexico that are not taxed by competing states. In making determinations regarding pyramiding, Mr. Eads indicated policymakers might consider the cost to the state's revenue stream, the type of relief that might be necessary and the kind of tax system that will ultimately benefit the state.

Committee members discussed the need for identification of industries that are most impacted by gross receipts tax pyramiding and whether reduced pyramiding should result at the cost of a narrowed tax base.

Tax Increment Financing

Raymond Sanchez, former speaker of the House of Representatives, introduced Robert Desiderio, former dean of the University of New Mexico School of Law, and Mike Daley, Mesa del Sol, to the committee. Mr. Desiderio explained the concept of tax increment financing (TIF) to the committee. He stated that TIF is an economic development tool for the financing of infrastructure. It facilitates taxable development by creating increased value within communities. From the increased value, increased property taxes and gross receipts taxes are expected to be generated. Those increased taxes, known as incremental revenues, are used to pay for public infrastructure projects. Mr. Desiderio indicated that 47 states use TIF programs to help communities generate value and add tax revenue collected from underutilized property. He further indicated that the legislature will be asked to approve legislation allowing local governments to use, at their option, an enhanced TIF in New Mexico. Mr. Desiderio stated that the TIF mechanism in the legislation will not reduce the amount of taxes presently received by local authorization. TIF directs the public purposes for which the revenue is used. TIF applies only to the incremental revenues that result from new development or redevelopment. Special TIF districts are proposed to be created through the legislation to administer incremental revenues, to issue bonds and to administer the infrastructure projects financed by TIF.

Mr. Daley provided the committee with examples of successful TIF projects throughout the country. He indicated that the infrastructure of Stapleton, a redevelopment of the former Denver airport, was accomplished through TIF. He further indicated that Anne Arundel County in Maryland used TIF to fund public infrastructure, transportation and utility improvements in connection with two major development projects. The Pittsburgh Technology Center in Pittsburgh, Pennsylvania, was also funded by TIF.

Mr. Desiderio and Mr. Daley provided the committee with a draft of the legislation, labeled as **draft 1**, that will serve as a basis for TIF discussions during the upcoming legislative session. David Buccholtz, attorney, Brownstein, Hyatt & Farber, LLP, answered committee member questions regarding the draft.

Questions and comments from the committee members addressed:

- the presence of a mill levy imposition component in the TIF discussion draft;
- the administrative implications of permitting TIF;
- whether business improvement district revenues might be pledged for a district created for TIF;
- whether funds raised by TIF would replace funds raised by impact fees;
- the consequences that might occur if a district created for TIF does not raise sufficient revenues to pay back bonds issued by the district;
- the distribution of tax revenues between a district created for TIF and a local governing body;
- whether the issuance of bonds for TIF would impact the New Mexico Finance Authority;
- voting implications in TIF districts comprised of government-owned land;
- mechanisms to fund elections for TIF districts; and
- whether revenues diverted to districts would adversely affect municipalities and counties.

Educational Retirement Fund Update

Greg Geisler, senior fiscal analyst, LFC, discussed the impact of the passage of 2005 Senate Bill 181 on the actuarial solvency of the Educational Retirement Fund. The legislation increases employer and employee contributions to the fund. The employer contribution will increase by .75 percent per year, amounting to a 5.25 percent increase over seven years. The employer contribution will increase from 8.65 percent in fiscal year 2005 to 13.9 percent in fiscal year 2012. The employee contribution will increase by .30 percent over four years. Thus, the contribution will increase from 7.6 percent in fiscal year 2005 to 7.9 percent in fiscal year 2009. The employer contribution increase is expected to generate $18.7 million during fiscal year 2007.

Mr. Geisler explained that since Senate Bill 181 became law, two developments have affected the Educational Retirement Fund. First, the Educational Retirement Board's fiscal year 2005 investment return of 9.86 percent exceeded its 8 percent target, which will result in improved solvency. However, the board has adjusted its actuarial assumptions, which has worsened its actuarial position as of June 30, 2004 from an unfunded actuarial liability of $2.4 billion to $2.6 billion. Assuming the six remaining years of employer contribution increases are implemented, the time frame for meeting actuarial benchmarks will change so that the board will reach an 80 percent funded ratio by 2020 rather than by 2019. Mr. Geisler indicated that since the impact of the recent developments is relatively small, Senate Bill 181 still improves the Educational Retirement Board's actuarial position, but he warned that improvement is not guaranteed.

Evalynne Hunemuller, director, Educational Retirement Board, discussed the impact of increased employee and employer contributions to the Educational Retirement Fund. She provided the committee with data regarding the funding ratios that would have resulted by 2025 if increased contributions to the fund had not been enacted versus the funding ratios expected to result from the enactment of increased contributions. The funding period, which before the enactment of the increased contributions stood at infinity, will decrease to the General Accounting Standard Board's recommended funding period of 30 years by 2012. The funding period is expected to decrease each year thereafter.

Questions and comments from the committee members addressed:

- the reason for a slight funding percentage dip expected in fiscal year 2007;
- the need to make educational retirement competitive with other states; and
- the possibility of encouraging longer work periods to improve Educational Retirement Fund solvency.

General Fund Consensus Revenue Estimates

James Jimenez, secretary, DFA, and Jan Goodwin, secretary, TRD provided the committee with the general fund consensus revenue estimates of the DFA and TRD. They first discussed the general economic outlook developed by the departments. According to Secretary Jimenez, inflation has risen since fiscal year 2003 but is expected to begin declining in fiscal year 2007. The federal funds rate continues to increase throughout the five-year forecast period. In addition, Secretary Jimenez noted that the New Mexico personal income tax revenue estimates were revised upward in fiscal year 2006. The estimates reflect improvements in wage and salary disbursements.

Natural gas prices were revised downward by $1.00 per million cubic feet (mcf) in fiscal year 2007 and oil prices were reduced by $2.00 per barrel in fiscal year 2006 and by $3.00 per barrel in fiscal year 2007. Several factors account for the revisions. First, supply is expected to increase so that hurricane losses will be offset by late next year. In addition, natural gas production in the Gulf of Mexico has been partially offset by increased imports. Demand has also decreased in response to increased prices. According to the DFA and TRD estimates, after peaking at over $10.00 per 1,000 cubic feet in October, New Mexico prices have fallen sharply relative to national average prices in recent weeks. The price reduction is partially due to a surplus of gas stemming from mild weather, production increases and limited pipeline outlets to eastern markets.

Secretary Goodwin provided a revenue outlook of the general fund for the upcoming fiscal years. Recurring general fund revenue is expected to total $5.385 billion in fiscal year 2006 and $5.232 billion in 2007. Those estimates reflect reductions from previous estimates by $95 million in fiscal year 2006 and $100.8 million in fiscal year 2007. The reductions reflect reduced natural gas prices.

Increases in gross receipts tax and personal income tax collections are also reflected in the new general fund revenue estimates. Revenue from the gross receipts tax was increased by $7.2 million in December. Personal income tax collections were increased by $11.6 million in fiscal year 2006 and by $6.4 million in fiscal year 2007.

The general fund revenue estimates also account for reduced motor vehicle and mineral production taxes. Motor vehicle excise tax revenue was reduced by $3.5 million in fiscal year 2006 and by $7.0 million in fiscal year 2007. Mineral production taxes and rents and royalties were collectively reduced by $121.8 million in fiscal year 2006 and by $137.7 million in fiscal year 2007 due to lower energy prices.

Increased expected earnings on state balances are additionally reflected in the estimates. Earnings on state balances were increased by $5.5 million in fiscal year 2006 and by $15.4 million in fiscal year 2007. Higher portfolio balances and an increasing federal funds rate indicate improved state earnings.

General fund balances are projected to reach 25.6 percent of recurring appropriations in fiscal year 2006. The fiscal year 2007 consensus forecast of $5.232 billion yields $523.6 million of "new money" when compared with fiscal year 2006 recurring appropriations of $4.709 billion.

David Abbey, director, LFC, provided the RSTPC members with an update of expected federal grants to the state. Due to projected decreases in some federal funds, state agencies have requested $11.2 million in fiscal year 2007 general fund dollars to replace those funds. Replacement requests have been made by courts, the first judicial district attorney, the Labor Department, the Children, Youth and Families Department, the Corrections Department and the Higher Education Department.

Mr. Abbey and Representative Luciano "Lucky" Varela, chair, LFC, stated that the legislature should exercise care in maintaining prudent expenditure levels in fiscal year 2007 and avoiding structural deficits in fiscal years 2008 and 2009.

Questions and comments from the committee members addressed:

- a potential decline in revenues and the need to keep expenditures at a manageable level; and
- whether tax rebates approved during the 2005 special session have been mailed out.

Alcohol Purchase Electronic Age Verification

Senator Cravens explained the role of a task force created pursuant to the passage of Senate Memorial 40 during the 2005 legislative session. The task force was charged with the responsibility of studying and investigating available and emerging technologies that verify the ages of retail alcohol customers. The task force concluded that additional tax credits for the purchase of electronic age verification equipment would encourage businesses to purchase such equipment. State law currently offers tax credits of $300 for each business location for which the electronic age verification equipment is used. On behalf of the task force, Senator Cravens presented a discussion draft, labeled as **draft 2**, that would raise the tax credit to $1,000 for each business location for which the age identification equipment is used.

Questions and comments from the committee members addressed:

- the cost of each electronic age verification device;
- locations at which electronic age verification equipment is used;
- whether electronic age verification equipment will store social security numbers;
- whether electronic age verification equipment will be able to detect fake identification cards; and
- the use of electronic age verification by large companies.

Credit for Produced Water

Tom Brown, Yates Petroleum Company, asked the committee to endorse legislation that would provide income tax credits to oil or gas well operators for water produced from oil or gas drilling.

Deduction for Fee-for-Service Providers and Underground Irrigation Systems Deduction

Amy Chavez, staff attorney, LCS, summarized the provisions of two of the discussion drafts requested by RSTPC members for consideration for RSTPC endorsement. The first draft, labeled as **draft 7**, provides for a gross receipts tax deduction for receipts from fee-for-service payments by health care practitioners, phased in over a period of five years. The second draft, labeled as **draft 9**, expands the scope of a gross receipts tax deduction for the sale of agricultural implements to include sales of underground irrigation tools, utensils and instruments. Sales of aboveground irrigation tools, utensils and instruments are currently eligible for the deduction.

Sithe Global and Dine Power Authority Proposal

Richard Minzner, lobbyist, Freddy Sanches, vice president, Sithe Global, LLC, and Steve Begaye, general manager, Dine Power Authority, urged the committee to endorse legislation to provide a partial credit against compensating tax owed with respect to a coal-fired electric generating facility located on Navajo Nation land. The credit is the lesser of: (1) 85 percent of the compensating tax owed with respect to the facility; or (2) the amount paid to the Navajo Nation in lieu of taxes, pursuant to an agreement between the taxpayer and the Navajo Nation. The draft presented was labeled as **draft 3**. According to Mr. Minzner, the proposal would provide approximately $50 million in tax relief.

Gross Receipts Tax Deduction for Hospital Construction

Representative Jose A. Campos asked the committee to endorse draft legislation, labeled as **draft 4**, to provide a gross receipts tax deduction for the sale of construction services, construction equipment and construction materials used to build a sole community provider hospital that is located in a federally designated health professional shortage area if the services or materials are sold to a foundation or nonprofit organization that enters into an agreement with a county to pay at least 95 percent of the costs of building the facility. Representative Campos indicated that the proposed deduction might serve as an incentive for the construction of hospitals in counties such as Guadalupe County.

Questions and comments from the committee members addressed:

- the wages that might be generated by hospitals for which construction services and materials may be deducted; and
- the age of the existing hospital in Guadalupe County.

Approval of Minutes

The minutes from the fifth meeting of the committee held on October 15 and 16 in Santa Fe were unanimously approved.

Biomass Gross Receipts Tax Deduction

Representative Hector Balderas and Art Hull, Public Service Company of New Mexico, asked the committee to endorse draft legislation, presented as **draft 5**, to expand a compensating tax deduction for biomass-related equipment to include deductions for feedstock processing or drying equipment, harvesting and transportation equipment, composting equipment or mulching equipment. It additionally creates a new gross receipts tax deduction for the sale of biomass materials and biomass-related equipment that mirrors the existing compensating tax deduction. Finally, the draft expands the definition of "biomass" of the renewable energy production tax credit to mirror the definition of biomass contained in the gross receipts and compensating tax deductions.

Thursday, December 1

Hospital Gross Receipts Tax Deduction

Cindy West, lobbyist, New Mexico For-Profit Hospitals, and Dan Weaks, lobbyist, New Mexico Hospitals and Health Systems Association, asked the committee to endorse draft legislation to provide a credit for the state portion of gross receipts tax for hospitals licensed by the Department of Health as presented in **draft 6**. Ms. West and Mr. Weaks indicated that the allowance of the credit would create greater tax parity among all hospitals. They further indicated that such a tax credit would encourage for-profit hospitals to expand services and improve facilities.

Questions and comments from the committee members addressed:

- whether the gross receipts tax is paid on the amounts collected or the amounts billed by hospitals;
- the administrative changes that might be involved in implementing the hold harmless provisions of the proposed draft; and
- the principle of tax policy that addresses the equal tax treatment of similar groups.

Local DWI Program Report

Tasia Young, legislative liaison, New Mexico Association of Counties (NMAC), and Rob Mitchell, NMAC DWI Affiliate, provided committee members with copies of a report by the NMAC DWI Affiliate regarding questions posed to the NMAC by the RSTPC throughout the interim regarding local DWI programs.

Chemical Gross Receipts Tax Deduction

Dan Najjar, lobbyist, and Terry McDermott, Intel, asked the committee to endorse legislation, as presented in **draft 8**, to provide for a deduction from gross receipts for sales of chemicals or reagents to manufacturers for use in the manufacturing process. The deduction is phased in over a period of three years. Mr. Najjar and Mr. McDermott indicated that the proposed draft could alleviate input costs for high-technology industries and could reduce gross receipts tax pyramiding.

Questions and comments from the committee members addressed:

- the potential benefit of the proposed draft to microelectromechanical systems companies;
- the difference between processing and manufacturing;
- the fiscal impact of the proposed draft;
- whether the proposed draft would attract new industries;
- the possibility of including a minimum requirement of chemicals purchased to narrow the scope of the proposed draft;
- whether industrial revenue bonds are being used to improve facilities throughout Sandoval County; and
- the number of distributors that would be affected with respect to Intel's use of the proposed draft.

Recycling Tax Incentives

Joseph Ellis, president, New Mexico Recycling Coalition (NMRC), and English Bird, executive director, NMRC, asked the committee to endorse draft legislation, presented as **draft**

10. The draft legislation provides for a gross receipts tax deduction for the sale of qualified recycling equipment approved by the Department of Environment.

Gross Receipts Tax Deduction for Professional Contests

Arturo Jaramillo, superintendent, Regulation and Licensing Department (RLD), asked the committee to endorse draft legislation, presented as **draft 33**, to provide for a deduction from gross receipts for the promotion of professional contests, including boxing, wrestling or martial arts contests. Superintendent Jaramillo indicated that professional contests in New Mexico have declined. Thus, fees used to support the New Mexico Athletic Commission from those professional contests have decreased. Superintendent Jaramillo indicated that declining revenues are threatening the continued existence of the commission. The RLD hopes that the proposed gross receipts tax deduction will aid in the attraction of professional contests to the state and improve the financial position of the commission.

Questions and comments from the committee members addressed:

- the number of boxing matches held on tribal land;
- the attendance at professional contests;
- the reason for the limited scope of the deduction;
- the possibility of increasing budget expenditures for the New Mexico Athletic Commission; and
- the possibility of the occurrence of boxing matches without supervision by an athletic commission.

Energy, Minerals and Natural Resources Department (EMNRD) Clean Energy Proposals

Craig O'Hare, special assistant for renewable energy, EMNRD, asked the committee to endorse draft legislation, labeled as **draft 12**, to provide for a tax credit for qualified energy generators that use solar-light or solar-heat-derived energy resources in the amount of $.02 per megawatt-hour for the first 200,000 megawatt-hours of electricity produced. The draft also expands the definition of "qualified energy generator" to include any facility that has at least one megawatt of energy generating capacity. The definition previously required at least 10 megawatts of energy generating capacity. The RSTPC endorsed a similar proposal made by the EMNRD during the 2004 legislative interim.

Advanced Energy Product Manufacturers Tax Credit

Representative Gonzales and Carol Radosevich, Public Service Company of New Mexico, asked the committee to endorse draft legislation to provide a tax credit for 5 percent of the costs of purchasing manufacturing equipment used to produce advanced energy products. The draft proposed is similar to House Bill 527 as amended during the 2005 legislative session, but broadens the scope of the definition of "advanced energy product" to include components for clean coal technology and renewable energy systems that generate bio-fuel. Questions and comments from the committee members addressed the need to provide incentives for research and development.

TRD Proposals

Dr. O'Donnell summarized the drafts presented by the TRD for endorsement by the committee.

Draft 13 requires the TRD to keep and to make available for public inspection records of tax credits made in excess of $10,000.

Draft 14 requires the TRD to mail assessments of taxes, interest, penalties and other payments to the last known mailing addresses of persons owing those payments. The draft further requires the TRD to notify persons who have claimed tax returns of the TRD's receipt of the claims. The draft also allows for protective claims.

Draft 15 repeals TRD authority to issue bulk fuel permits that enable farmers and contractors to buy clear diesel fuel for off-road use.

Draft 17 requires sellers of cigarettes to file information returns with the TRD. The information returns will require information on cigarette imports into and exports from the state and on cigarette sales to tribes and retailers. A penalty of $250 is included for failure to file a timely information return. The draft also increases a penalty on unstamped cigarettes to 100 percent of the cigarette tax due plus $500.

Draft 18 empowers the TRD to contract with collection agencies to collect or assist in the collection of an obligation over 120 days past due to the state or a political subdivision of the state pursuant to the state's tax laws. It also expands the tax programs under which electronic reporting may be required by the TRD. Draft 18 was withdrawn from consideration by the TRD.

Draft 19 requires tax return preparers who file over 25 personal income tax returns to file those returns electronically, unless the person for whom the return is prepared elects to file a return by other means. The draft also gives the TRD discretion in establishing a due date for withholding tax payments.

Draft 20 caps the penalty imposed for incorrect reporting of gross receipts tax deductions for the sale of food or medical services to a maximum of $10,000. The requirement for validating gross receipts tax deductions of sales-for-resale is also loosened to allow for evidence other than a type-2 nontaxable transaction certificate.

Draft 21 permits the TRD to inform a licensing body of licensee failure to file or pay taxes and other relevant taxpayer information for use in disciplinary proceedings. It also provides the failure to file a tax return as grounds for suspension or revocation of occupational licenses and for the disbarment of attorneys.

Draft 22 extends the time period during which managed audit participants may make interest-free payments on delinquent taxes from 30 days to 180 days. The draft further eliminates for managed audit participants the penalty for incorrect reporting of gross receipts tax deductions for sales of food or health care practitioner services. It also extends the time period during which an income tax form may be filed due to receipt of an extension for filing the federal income tax form. The time period is extended from four to six months.

Draft 23 increases the civil penalty for failure to pay or file a tax return from 2 percent per month, capped at a total of 10 percent, to 2 percent per month, capped at a total of 16 percent. The draft also decreases the interest rate charged on underpayments and overpayments of tax from 15 percent annually to the rate used by the Internal Revenue Service (IRS). The IRS rate is calculated as the federal short-term interest rate plus 3 percent. It is currently equal to 7 percent annually.

Draft 24 makes a technical change to income tax exemption for low- and middle-income taxpayers enacted in 2005 to make the phase-out of the benefits more gradual. According to the TRD, the law that passed inadvertently contained an abrupt elimination of tax benefits at $40,667, so that a $1.00 increase in income would result in a $50.00 increase in taxes.

Draft 25 provides a technical change to expand a special fuel excise tax deduction for school bus operators that contract with the Public Education Department so that the same deduction can be taken by school bus operators that contract with public school districts.

Draft 26 creates an electronic reporting requirement for holders of more than 25 unclaimed properties presumed abandoned. It permits the sale of abandoned property to occur by any reasonable method and extends the time period during which an owner can enter into an agreement to locate abandoned property from 24 months to 48 months.

Draft 27 permits the TRD to disclose personal income tax information to the Bureau of Business and Economic Research of the University of New Mexico for the purposes of population and demographic research. The bureau is prohibited from releasing that information in any form other than as statistics that protect taxpayer identity. The draft also permits the TRD to disclose taxpayer information to law enforcement agencies with which the department is conducting a joint investigation.

New Mexico Municipal League Proposals

Bill Fulginiti, executive director, New Mexico Municipal League (NMML), summarized the bills recommended by the NMML for endorsement.

Draft 28 permits municipalities and counties to obtain access to information on gross receipts taxes and gross receipts taxes paid.

Draft 29 requires that certain collections by the Aviation Division of the Department of Transportation be distributed to the State Aviation Fund. The draft also provides for distributions to the State Aviation Fund from the general fund in an amount equal to $80,000 monthly from July 1, 2006 to June 30, 2007; $167,000 monthly from July 1, 2007 through June 30, 2008; and $250,000 monthly after June 30, 2008.

Draft 30 permits municipalities to trade a part of the municipal distribution of the gross receipts tax for a distribution of personal income tax. Draft 30 was withdrawn from consideration by the NMML.

Draft 31 allows county and municipal governments to impose a local option compensating tax. The local option compensating tax is proposed to be imposed in addition to local option gross receipts taxes. The draft requires the TRD to administer the tax and to transfer payments to local governments.

Draft 32 provides for a municipal property tax rebate for low-income homeowners and permits municipalities to submit to qualified electors the question of a new property tax imposition.

Votes on Proposed Legislation for Committee Endorsement

The committee members reviewed each piece of legislation presented and voted whether to endorse the legislation. The table on the following pages indicates the draft number, description and proponent of each piece of legislation and the committee's final vote for or against endorsement of that legislation. Committee sponsors for the endorsed bills are also listed.

REVENUE STABILIZATION AND TAX POLICY COMMITTEE
LEGISLATION PROPOSALS
NOVEMBER 30-DECEMBER 1

Draft Number	**Title**	**Agency/ Proponent(s)**	**202 Number**	**Vote In Favor**	**Vote Against**	**Endorsement (Y/N)**	**Sponsor(s)**
1	Tax Increment Financing	Sanchez/ Desiderio/ Daley	N/A	8	4	Y, in concept	Rep. Taylor Rep. Lujan Sen. Snyder
2	GRT Ded. for Electronic Purchase Age Verification Equip.	Sen. Cravens	159286.1	11	1	Y	Sen. Cravens
3	Coal Facility Comp. Tax Credit	Sithe Global/ Dine Power Authority	158616.3	11	1	Y	Rep. Taylor
4	GRT Ded. for Hospital Construction	Rep. Jose A. Campos	159263.1	12	0	Y, as amended	Rep. Hanosh
5	Biomass GRT Ded.	Rep. Hector Balderas/ PNM	159287.2	12	0	Y, as amended	Rep. Crook Sen. Cisneros

Draft Number	Title	Agency/ Proponent(s)	202 Number	Vote In Favor	Vote Against	Y/N Endorsed	Sponsor(s)
6	Hospital Service GRT Ded.	NM For-Profit Hospitals/NM Hospital Association	159130.2	12	0	Y	Sen. Smith
7	GRT Ded for Medical Service Providers	RSTPC Request	159284.1	12	0	Y	Sen. Taylor
8	Chemical GRT Ded.	Intel	N/A	12	0	Y	Rep. Lujan Sen. Altamirano Sen. Rodriguez
9	Underground Irrigation Systems Ded.	RSTPC Request	159281.1	12	0	Y	Rep. Taylor Sen. Taylor
10	Recycling Tax Ded.	NM Recycling Coalition	159235.1	3	9	N	None
11	Tax Credit for Private Schools	RSTPC Request	159280.1	5	7	N	None

Draft Number	Title	Agency/ Proponent(s)	202 Number	Vote In Favor	Vote Against	Y/N Endorsed	Sponsor(s)
12	Renewable Energy Production Credit Amendments	EMNRD	159236.1	12	0	Y, as amended	Sen. Cisneros
13	Public Record Tax Credits	TRD	159052.2	12	0	Y	Rep. Arnold-Jones Rep. Whitaker Sen. Altamirano
14	Assessments & Protective Claims	TRD	159053.2	12	0	Y	Rep. Arnold-Jones Rep. Whitaker Sen. Altamirano
15	Repeal Bulk Fuel Permits	TRD	159054.1	12	0	Y	Rep. Gonzales
No Draft 16							
17	Cigarette Tax Law Enforcement	TRD	159056.3	12	0	Y	Rep. Crook
18	Contracts to Collect Aged Receivables	TRD	159057.1	N/A	N/A	Withdrawn by TRD	None

Draft Number	Title	Agency/ Proponent(s)	202 Number	Vote In Favor	Vote Against	Y/N Endorsed	Sponsor(s)
19	Electronic Filing Requirements	TRD	159058.1	12	0	Y	Rep. Arnold-Jones Rep. Whitaker Sen. Altamirano
20	GRT Ded. Documenting Reform	TRD	159059.2	12	0	Y	Rep. Arnold-Jones Rep. Whitaker Sen. Altamirano
21	Tax Compliance & Fraud Reforms	TRD	159060.2	12	0	Y	Rep. Arnold-Jones Rep. Whitaker Sen. Altamirano
22	Managed Audit Improvement	TRD	159061.2	12	0	Y	Rep. Arnold-Jones Rep. Whitaker Sen. Altamirano
23	Penalties & Interest	TRD	159062.1	12	0	Y	Rep. Arnold-Jones Rep. Whitaker Sen. Altamirano
24	2005 PIT Cleanup	TRD	159063.1	12	0	Y	Rep. Arnold-Jones Rep. Whitaker Sen. Altamirano
25	School Bus Fuel Relief Cleanup	TRD	159064.1	12	0	Y	Rep. Arnold-Jones Rep. Whitaker Sen. Altamirano

Draft Number	Title	Agency/ Proponent(s)	202 Number	Vote In Favor	Vote Against	Y/N Endorsed	Sponsor(s)
26	Unclaimed Property Amendments	TRD	159065.1	12	0	Y	Rep. Arnold-Jones Rep. Whitaker Sen. Altamirano
27	Taxpayer Information Disclosure	TRD	159342.1	12	0	Y, as amended	Rep. Arnold-Jones Rep. Whitaker Sen. Altamirano
28	Municipality & County GRT Info. Disclosure	NMML	159291.2	12	0	Y	Sen. Altamirano
29	Dist. to Aviation Fund	NMML	159292.1	12	0	Y	Rep. Lujan Sen. Altamirano
30	Trade GRT for PIT Distribution	NMML	159266.2	N/A	N/A	Withdrawn by NMML	None
31	Local Option Comp. Tax	NMML	159265.1	12	0	Y	Rep. Gonzales Rep. Silva
32	Municipal Property Tax Rebate	NMML	159293.1	11	1	Y	Rep. Gonzales Sen. Taylor

Draft Number	Title	Agency/ Proponent(s)	202 Number	Vote In Favor	Vote Against	Y/N Endorsed	Sponsor(s)
33	Production or Staging of Professional Contests	RLD	158991.1	8	4	Y	Rep. Saavedra
---	Produced Water Tax Credit	Yates Petroleum	N/A	12	0	Y	Rep. Hanosh
---	Advanced Energy Products Tax Credit	RSTPC Request	159362.1	12	0	Y	Rep. Gonzales