REVENUE STABILIZATION AND TAX POLICY COMMITTEE

2010 INTERIM

Prepared by the Legislative Council Service
Staff
Pamela Ray, Staff Attorney
Doris Faust, Staff Attorney
Ric Gaudet, Staff

REVENUE STABILIZATION AND
TAX POLICY COMMITTEE

2010 Interim

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REVENUE STABILIZATION AND
TAX POLICY COMMITTEE

Section 1

2010
Introduction

2010 Interim

Revenue Stabilization and Tax Policy Committee
Representative Edward C. Sandoval, Chair
Senator John Arthur Smith, Vice Chair

SUMMARY OF WORK COMPLETED
2010 Interim

The Revenue Stabilization and Tax Policy Committee held seven meetings in 2010. The December meeting was a one-day meeting. The committee was asked by the Government Restructuring Task Force to review several agencies for possible economies that could be achieved, but the agencies clearly needed to maintain personnel and funding to perform their assigned duties. The Taxation and Revenue Department is responsible for collection of most of the tax revenue funding the state. It is therefore of paramount importance that the agency be able to collect, audit and enforce the taxation laws of the state to maximize collections at this time. The Department of Transportation presented information that concerned the committee a great deal regarding the condition of the state's roads if funding to maintain them is not available soon. The Motor Transportation Division of the Department of Public Safety also left the committee with the understanding that it provides services that aid in the collection of trip taxes, weight-distance taxes and other various fees that both are channeled to the State Road Fund or to the general fund.

Dorothy "Duffy" Rodriguez, the new secretary-designate of taxation and revenue, started with the department in late June. Secretary-Designate Rodriguez came to her first Revenue Stabilization and Tax Policy Committee meeting after only her fifth day in that position. The department, nonetheless, was able to generate a chart of tax credits, deductions and exemptions, with other tax exceptions or exclusions included. The document provided the expenditure on each tax benefit made by the state. The committee reviewed the economic development credits closely but was unable to look closely at the several low- and middle-income family tax benefits to determine how successful those benefits are. It was determined that without a clearly stated and measurable purpose, analyzing the effectiveness of most tax benefits was not possible. The committee decided to put tax credits on a review schedule that would allow time for the departments with the most information about the credits to begin gathering data on the use of those credits.

Because this was an election year, the department did not suggest legislation for the upcoming 2011 session. The committee reviewed 14 bills and endorsed 9. The list of bills endorsed and reviewed can be found in Section 10 of this report.

REVENUE STABILIZATION AND
TAX POLICY COMMITTEE

Section 2

2010 INTERIM
Proposed and Approved
Work Plan
Schedule
Budget

2010 PROPOSED
WORK PLAN, MEETING SCHEDULE AND BUDGET
for the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

Members

Rep. Edward C. Sandoval, Chair
Sen. John Arthur Smith, Vice Chair
Sen. Carlos R. Cisneros
Rep. Nathan P. Cote
Rep. Anna M. Crook
Sen. Dianna J. Duran
Sen. Tim Eichenberg
Rep. Keith J. Gardner
Sen. Timothy Z. Jennings
Sen. Timothy M. Keller
Sen. Gay G. Kernan
Rep. Ben Lujan
Rep. Rodolpho "Rudy" S. Martinez
Sen. Howie C. Morales
Rep. Henry Kiki Saavedra
Sen. William E. Sharer
Rep. Thomas C. Taylor
Rep. Jim R. Trujillo

Designees

Rep. Ray Begaye
Sen. Mark Boitano
Rep. Donald E. Bratton
Rep. Zachary J. Cook
Sen. Kent L. Cravens
Rep. Miguel P. Garcia
Sen. Phil A. Griego
Sen. Clinton D. Harden, Jr.
Rep. Sandra D. Jeff
Sen. Carroll H. Leavell
Rep. Antonio "Moe" Maestas
Sen. Steven P. Neville
Rep. Debbie A. Rodella
Sen. Nancy Rodriguez
Sen. Bernadette M. Sanchez
Sen. John M. Sapien
Rep. James R.J. Strickler
Rep. Don L. Tripp
Rep. Luciano "Lucky" Varela
Sen. Peter Wirth

Proposed Work Plan for 2010

The Revenue Stabilization and Tax Policy Committee 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... ".

A. In the 2010 interim, the committee will:

1. examine state taxes and discuss each tax based on sound tax policy principles and the contribution to state revenue made by each tax;

2. review the revenue status of the state, examine the implementation and effectiveness of revenue enhancement methods already adopted and discuss the need and opportunities for further revenue enhancement;

3. continue to review the effectiveness and value to the state of tax incentives and review exemptions, deductions and credits to determine the state's ability to track and identify

methods to determine value;

4. review the implementation and effect of the tax amnesty program and identify taxes where amnesty was most heavily used by taxpayers, and follow the implementation of the gaming tax credit and the business retention gross receipts tax;

5. examine the effectiveness and efficiency of appropriations and revenue generation programs in the Taxation and Revenue Department and other departments in the state that generate revenue to determine if such funds are fully used for the purposes for which they were raised;

6. identify methods of obtaining data and information on a more timely basis;

7. review trends in state investment earnings; and

8. respond to the requests of the Government Restructuring Task Force.

B. Other matters that will be addressed by the committee include:

1. ongoing property tax issues;

2. the relative costs and benefits of holding local governments harmless when the legislature reduces gross receipts taxes;

3. the effectiveness of collecting the weight-distance tax after recent cuts to the Department of Public Safety and a review of balances in the State Road Fund;

4. use of industrial revenue bonds in the state including revenue lost and value of the benefits gained by local communities;

5. a review of oversight of and access to data from local gross receipts tax collections and distributions;

6. the progress of implementation of the solar energy loan districts;

7. New Mexico's ability to tax internet transactions; and

8. the balances in and performance of severance tax and land grant permanent funds and the revenue from gaming in New Mexico.

2010 Proposed Meeting Schedule and Budget

The dates on which the Revenue Stabilization and Tax Policy committee has proposed to meet are:

Date	Location		Proposed Budget
June 7 (M)	Santa Fe, State Capitol, Room 307		$ 8,856
July 8-9 (Th-F)	Santa Fe, State Capitol, Room 322		11,500
August 23-24 (M-Tu)	Santa Fe, State Capitol, Room 322		11,500
September 14-15 (Tu-W)	Santa Fe, State Capitol, Room 322		10,600
October 25-26 (M-Tu)	Santa Fe, State Capitol, Room 322		10,600
November 29-30 (M-Tu)	Santa Fe, State Capitol, Room 322		10,600
December 15 (W)	Santa Fe, State Capitol, Room 307		7,643
		TOTAL:	$71,299*

*This committee has designees rather than advisory members. All per diem and mileage reimbursement for members and designees come from the committee's budget.

2010 APPROVED
WORK PLAN AND MEETING SCHEDULE
for the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

Members

Rep. Edward C. Sandoval, Chair
Sen. John Arthur Smith, Vice Chair
Sen. Carlos R. Cisneros
Rep. Nathan P. Cote
Rep. Anna M. Crook
Sen. Dianna J. Duran
Sen. Tim Eichenberg
Rep. Keith J. Gardner
Sen. Timothy Z. Jennings
Sen. Timothy M. Keller
Sen. Gay G. Kernan
Rep. Ben Lujan
Rep. Rodolpho "Rudy" S. Martinez
Sen. Howie C. Morales
Rep. Henry Kiki Saavedra
Sen. William E. Sharer
Rep. Thomas C. Taylor
Rep. Jim R. Trujillo

Designees

Rep. Ray Begaye
Sen. Mark Boitano
Rep. Donald E. Bratton
Rep. Zachary J. Cook
Sen. Kent L. Cravens
Rep. Miguel P. Garcia
Rep. Roberto "Bobby" J. Gonzales
Sen. Phil A. Griego
Sen. Clinton D. Harden, Jr.
Rep. Sandra D. Jeff
Sen. Carroll H. Leavell
Rep. Antonio "Moe" Maestas
Sen. Steven P. Neville
Rep. Debbie A. Rodella
Sen. Nancy Rodriguez
Sen. Bernadette M. Sanchez
Sen. John M. Sapien
Rep. James R.J. Strickler
Rep. Don L. Tripp
Rep. Luciano "Lucky" Varela
Sen. Peter Wirth

Proposed Work Plan for 2010

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3. continue to review the effectiveness and value to the state of tax incentives and

review exemptions, deductions and credits to determine the state's ability to track and identify methods to determine value;

4. review the implementation and effect of the tax amnesty program and identify taxes where amnesty was most heavily used by taxpayers, and follow the implementation of the gaming tax credit and the business retention gross receipts tax;

5. examine the effectiveness and efficiency of appropriations and revenue generation programs in the Taxation and Revenue Department and other departments in the state that generate revenue to determine if such funds are fully used for the purposes for which they were raised;

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4. use of industrial revenue bonds in the state including revenue lost and value of the benefits gained by local communities;

5. a review of oversight of and access to data from local gross receipts tax collections and distributions;

6. the progress of implementation of the solar energy loan districts;

7. New Mexico's ability to tax internet transactions; and

8. the balances in and performance of severance tax and land grant permanent funds and the revenue from gaming in New Mexico.

Revenue Stabilization and Tax Policy Committee
2010 Approved Meeting Schedule

The dates on which the Revenue Stabilization and Tax Policy committee has proposed to meet are:

Date	Location
June 7 (M)	Santa Fe, State Capitol, Room 307
July 8-9 (Th-F)	Santa Fe, State Capitol, Room 322
August 23-24 (M-Tu)	Santa Fe, State Capitol, Room 322
September 14-15 (Tu-W)	Santa Fe, State Capitol, Room 322
October 25-26 (M-Tu)	Santa Fe, State Capitol, Room 322
November 29-30 (M-Tu)	Santa Fe, State Capitol, Room 322
December 15 (W)	Santa Fe, State Capitol, Room 307

REVENUE STABILIZATION AND
TAX POLICY COMMITTEE

Section 3

June 2010
Agenda
Minutes

Revised: June 4, 2010

TENTATIVE AGENDA
for the
FIRST MEETING IN 2010
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

June 7, 2010
Room 307, State Capitol

<u>Monday, June 7</u>

10:00 a.m.	**Call to Order** —Representative Edward C. Sandoval, Chair
10:05 a.m.	**Coordination with the Government Restructuring Task Force and Other Administrative Issues** —John Yaeger, Assistant Director, Legislative Council Service (LCS)
10:30 a.m.	**Post-Session Fiscal Review** —Tom Clifford, Chief Economist, Legislative Finance Committee
11:30 a.m.	**Approval of Committee Work Plan and Meeting Schedule** —Pam Ray, Staff Attorney, LCS —Doris Faust, Staff Attorney, LCS
12:00 noon	**Tax Legislation Review** —Marilyn Hill, Deputy Secretary, Taxation and Revenue Department (TRD) —Al Maury, Temporary Chief Economist, TRD
1:00 p.m.	**Adjourn**

MINUTES
of the
FIRST MEETING IN 2010
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

June 7, 2010
Room 307, State Capitol
Santa Fe

The first meeting of the Revenue Stabilization and Tax Policy Committee (RSTP) for 2010 was called to order by Representative Edward C. Sandoval, chair, at 10:12 a.m. in Room 307 of the State Capitol in Santa Fe

Present
Rep. Edward C. Sandoval, Chair,
Sen. John Arthur Smith, Vice Chair
Rep. Nathan P. Cote
Rep. Anna M. Crook
Sen. Dianna J. Duran
Rep. Keith J. Gardner
Sen. Timothy Z. Jennings,
Sen. Gay G. Kernan
Rep. Ben Lujan, Speaker of the House
Rep. Rodolpho "Rudy" S. Martinez
Sen. Howie C. Morales
Rep. Henry Kiki Saavedra
Sen. William E. Sharer
Rep. Thomas C. Taylor
Rep. Jim R. Trujillo

Absent
Sen. Carlos R. Cisneros
Sen. Tim Eichenberg
Sen. Timothy M. Keller

Designees
Rep. Antonio "Moe" Maestas (guest)
Sen. Nancy Rodriguez

Rep. Ray Begaye
Sen. Mark Boitano
Rep. Donald E. Bratton
Rep. Zachary J. Cook
Sen. Kent L. Cravens
Rep. Miguel P. Garcia
Sen. Clinton D. Harden, Jr.
Rep. Sandra D. Jeff
Sen. Carroll H. Leavell
Sen. Steven P. Neville
Rep. Debbie A. Rodella
Sen. Bernadette M. Sanchez
Sen. John M. Sapien

Rep. James R.J. Strickler
Rep. Don L. Tripp
Rep. Luciano "Lucky" Varela
Sen. Peter Wirth

Staff
Pam Ray, Staff Attorney, Legislative Council Service (LCS)
Doris Faust, Staff Attorney, LCS
Ric Gaudet, Research and Committee Staff, LCS

Monday, June 7

Coordination with the Government Restructuring Task Force (GRTF) and Other Administrative Issues

Paula Tackett, director, LCS, briefed the committee on directives from the New Mexico Legislative Council to interim committees. The council wants to significantly reduce executive and legislative staff travel expenses during the interim. Committees have been directed to meet in Santa Fe, and the number of meeting days for most committees has been reduced.

The GRTF has requested that interim committees report their recommendations about specific restructuring ideas for the departments under their area of study. Ms. Tackett said that interim committees should make their recommendations to the GRTF as soon as possible so that the task force can make effective restructuring recommendations to the legislature.

A committee member cautioned fellow legislators about travel expenses. He said there may not be enough money to pay for regular committee expenses if members have significant out-of-state travel expenses this year.

A committee member said the GRTF is studying many short-term and long-term solutions to the government structure issue. Some of the long-term solutions would require constitutional amendments; however, there are short-term ideas to increase efficiency. One example would be to make the magistrate court a court of record for DWI cases, which could save money and make the court system much more efficient.

A committee member asked if a regulatory reform committee would be appointed during the 2010 interim. Ms. Tackett said that the New Mexico Legislative Council did not create that committee, but it may do so at the June 29 meeting.

Representative Sandoval thanked Ms. Tackett for her many years of service, and the committee and audience gave the retiring director a standing ovation to express their gratitude for her service.

Post-Session Fiscal Review

Tom Clifford, chief economist, Legislative Finance Committee (LFC), provided the committee with an update of New Mexico's fiscal picture since the end of the 2010 legislative sessions. He began by reviewing the LFC's adopted tax policy principles and the cumulative annual impacts of significant general fund tax measures since 2003, which in fiscal year 2011 will decrease revenues by $420 million. Prior to the start of the session, the cumulative annual decrease was predicted to be $600 million. Mr. Clifford identified other areas in which the state could increase revenue and described the fiscal impact of the 2010 Senate Bill 248, which would have eliminated or reduced the amount of available tax credits and exemptions for certain activities. The increased revenue from that bill would have been $45 million in fiscal year 2011.

Mr. Clifford reviewed recent U.S. and New Mexico economic indicators. Although the nationwide economic outlook has improved slightly since December 2009, New Mexico has lagged behind in the recovery. However, the state's personal income growth has shown signs of improvement, predicted to be 3.3 percent this year, and New Mexico's job losses bottomed out in January 2010. Taxable gross receipts have also shown strong growth since March, which could be the beginning of an economic rebound, said Mr. Clifford.

Oil price futures for July are currently trading at $72.00 per barrel, which is close to the December 2009 consensus revenue group's estimate of $75.00. Natural gas futures are also trading at $4.80, much higher than this time last year. Additionally, there has been an increase in the price of natural gas liquids, which has encouraged more gas production in the state.

Corporate earnings have fallen more than 50 percent since 2007 but appear to be slowly rebounding for fiscal year 2011. Tax credits, especially the film production tax credit, have accounted for much of the drop in state corporate income tax (CIT) collections in the past three years.

While the past two fiscal years have seen large revenue decreases, fiscal year 2011 is predicted to show a six percent increase, but the previous high revenues in fiscal year 2008 are not expected to return until fiscal year 2015. Fiscal year 2011 growth is expected to be from many sectors, including a large increase from oil and gas revenues.

The LFC's revenue tracking has shown a total of $46 million less in total revenue than was predicted in the December 2009 forecast. While oil and gas revenues have performed better than expected, gross receipts tax (GRT) and CIT revenues are far below projections. Personal income tax (PIT) revenues are only slightly below projections, said Mr. Clifford.

Mr. Clifford then compared budgeted state expenditures for fiscal year 2011 to previous years. Public school spending declined 1.8 percent from fiscal year 2010 and 5.7 percent from fiscal year 2009. Higher education spending declined 3.5 percent and 7.4 percent, respectively. Medicaid spending was reduced only slightly from the previous two years, and other agencies have seen 12 percent reductions. Many revenue measures were enacted during the regular and special sessions, with a fiscal year 2011 impact projected to be

$173 million. Fiscal year 2010 is expected to have year-end reserves of 5.2 percent, which is a decrease of more than $500 million. Reserves would have fallen well below zero but for the $1.1 billion in solvency measures enacted in the past few sessions. In addition, if the federal government does not extend the enhanced matching formula for Medicaid funding, the state's reserves will again be at risk.

The challenges facing policymakers in developing the fiscal year 2012 budget are many. Assuming six percent growth in revenues over fiscal year 2011 and added revenue from recently enacted provisions, the state should generate $5.6 billion in general fund revenue. However, the state still needs to replace nearly $500 million in one-time funds and savings and would face a $236 million shortfall, assuming a flat budget from fiscal year 2011.

A committee member said that many businesses in Roswell have reported gross receipts 11 percent lower than last year. He questioned whether New Mexico's economy has yet reached the bottom of the recession. Another legislator agreed and said that the Farmington economy, based mostly on gas production, usually lags behind the rest of the state. Currently, there are only nine active gas rigs in the state, but 45 are needed just to maintain the current gas flow.

Mr. Clifford was asked to research whether the increase in copper prices will bring job growth to the southwestern part of New Mexico.

A committee member asked whether the recent growth in jobs is a reflection of hiring by the U.S. Census Bureau. Mr. Clifford said that the jobs numbers do not reflect an increase in hiring by the private sector.

A committee member commented that the economic woes of Greece, which he said were caused by pensions that are too generous, could be a lesson for New Mexico, which also has generous pensions for its public sector. Public employees in some cases can work for 20 years and then receive a pension for the next 40 years.

Mr. Clifford was asked whether any changes in federal law regarding internet sales are expected this year. Mr. Clifford said that the committee should revisit this issue and that New Mexico may have a better legal basis to collect the GRT on internet sales than other states because of the nature of the tax.

Approval of Committee Work Plan and Meeting Schedule

Ms. Ray presented to the committee a proposed work plan and meeting schedule for the 2010 interim. The committee's work plan has been reduced from the 2009 plan, due to the New Mexico Legislative Council directive to reduce the number of interim committee meeting days. After discussion and the addition of a few more items to study, the committee adopted its work plan as follows:

A. In the 2010 interim, the committee will:

1. examine state taxes and discuss each tax based on sound tax policy principles and the contribution to state revenue made by each tax;

2. review the revenue status of the state, examine the implementation and effectiveness of revenue enhancement methods already adopted and discuss the need and opportunities for further revenue enhancement;

3. continue to review the effectiveness and value to the state of tax incentives and review exemptions, deductions and credits to determine the state's ability to track and identify methods to determine value;

4. review the implementation and effect of the tax amnesty program and identify taxes where amnesty was most heavily used by taxpayers, and follow the implementation of the gaming tax credit and the business retention GRT;

5. examine the effectiveness and efficiency of appropriations and revenue generation programs in the Taxation and Revenue Department (TRD) and other departments in the state that generate revenue to determine if such funds are fully used for the purposes for which they were raised;

6. identify methods of obtaining data and information on a more timely basis;

7. review trends in state investment earnings; and

8. respond to the requests of the GRTF.

B. Other matters that will be addressed by the committee include:

1. ongoing property tax issues;

2. the relative costs and benefits of holding local governments harmless when the legislature reduces GRTs;

3. the effectiveness of collecting the weight-distance tax after recent cuts to the Department of Public Safety and a review of balances in the State Road Fund;

4. use of industrial revenue bonds in the state, including revenue lost and the value of the benefits gained by local communities;

5. a review of oversight of and access to data from local GRT collections and distributions;

6. the progress of implementation of the solar energy loan districts;

7. New Mexico's ability to tax internet transactions; and

8. the balances in and performance of severance tax and land grant permanent funds and the revenue from gaming in New Mexico.

The committee adopted its proposed schedule, with the direction that staff research the extra costs associated with holding its August meeting in Rio Rancho. The dates on which the RSTP has proposed to meet are:

Date	Location
June 7 (M)	Santa Fe, State Capitol, Room 307
July 8-9 (Th-F)	Santa Fe, State Capitol, Room 322
August 23-24 (M-Tu)	Santa Fe, State Capitol, Room 322
September 14-15 (Tu-W)	Santa Fe, State Capitol, Room 322
October 25-26 (M-Tu)	Santa Fe, State Capitol, Room 322
November 29-30 (M-Tu)	Santa Fe, State Capitol, Room 322
December 15 (W)	Santa Fe, State Capitol, Room 307

Tax Legislation Review

Marilyn Hill, deputy secretary, TRD, and Al Maury, acting chief economist, TRD, reviewed for the committee tax laws enacted during the 2010 legislative sessions. Ms. Hill first updated the committee on ongoing TRD programs, including the provision of courtesy lines at Motor Vehicle Division offices for elderly and disabled persons; the increased requirements for certain taxpayers to file tax returns electronically, which will greatly speed up the department's data reporting; and the tax amnesty program, which is in effect starting today and is expected to bring in more revenue to the state. She clarified that the amnesty program does not apply to existing liabilities; it only applies to tax payments that have not yet been identified.

Mr. Maury reviewed the tax law, motor vehicle and other changes enacted by the legislature during the regular and special sessions. The legislation includes:

- approval of the Las Cruces tax increment development district and authority for the district to issue $75 million in bonds;

- a memorial requesting the TRD to aggressively enforce GRT laws and collect GRTs;

- the establishment of a temporary tax amnesty program to allow taxpayers to pay taxes that would otherwise be late without the accrual of penalties or interest;

- the elimination of the state and local income tax deduction from the calculation of New Mexico income tax due, which had been seen as an unfair double deduction for higher-income taxpayers;

- the requirement that certain pass-through entities remit oil and gas withholding tax payments and other payments to the state, which has an estimated positive fiscal impact to the state of $10 million annually;

- the increase of the state GRT by one-eighth percent to 5.125 percent;

- the provision of an advanced energy deduction to be taken against gross receipts and compensating tax due for certain types of eligible costs associated with renewable and clean coal energy production facilities;

- approval of a new local option business retention GRT and a corresponding gaming tax credit, designed to help Ruidoso Downs continue its racetrack operations by reducing the amount of gaming tax it pays to the state in exchange for a countywide GRT that is partially shared with the state;

- the loosening of restrictions on which counties are able to impose a capital outlay GRT;

- allowing counties to pledge the one-sixteenth increment of the county GRT to the payment of bonds currently authorized by Section 4-62-1 NMSA 1978;

- expansion of the allowable uses of the county hospital emergency GRT to include the construction of county hospitals and acquiring associated land and buildings;

- the increase of the compensating tax on using tangible property in New Mexico from five percent to 5.125 percent. The compensating tax on the use of services rendered in New Mexico, however, remains at five percent;

- the imposition of the compensating tax on certain out-of-state businesses that are determined to have nexus in New Mexico;

- the expansion to all counties of the use of affordable housing tax credits;

- the provision of an agricultural biomass tax credit of $5.00 per wet ton of material transported to a qualified biomass energy production facility;

- a memorial supporting the bond election of the Albuquerque Public Schools;

- a proposal to amend the Constitution of New Mexico to exempt from property taxation property owned by veterans' organizations;

- the exclusion from consideration of "physical improvements" to property for property tax assessment purposes of certain solar energy or heat systems to residential property;

- increasing the distribution of the oil and gas conservation tax to the Oil and Gas Reclamation Fund and increasing the rate of the tax to .24 percent when the average price of oil reaches a threshold of $70.00 per barrel;

- increasing the cigarette tax by $.75 per pack and providing for tribal governments to maintain the current $.91 differential between tribal and non-tribal sales. The law was passed by the legislature to be temporary and to distribute a portion of the revenue for education and youth services, but the governor's line-item vetoes made the increase permanent, distributed all of the increase to the general fund and repealed existing law that distributed a portion of the tax to municipalities and counties;

- providing for interlock device fees for DWI offenders to partially offset the device costs for indigent offenders;

- a memorial asking for the study of antabuse as an alternative to ignition interlock devices;

- requiring training for law enforcement officers about parking access for persons with disabilities;

- allowing the renewal of driver's licenses by telephone or other electronic means;

- the imposition of a magistrate courts operations fee of $4.00 to be imposed on penalty assessment misdemeanors;

- enacting the Colonias Infrastructure Act and providing an annual severance tax bond issuance of five percent of bonding capacity, plus an annual distribution of $10 million from the newly created (yet not funded) Colonias Infrastructure Trust Fund, beginning in fiscal year 2012;

- extension of tribal gasoline tax-sharing agreements from 10 to 20 years;

- enacting the Sunshine Portal Transparency Act, which requires the Department of Information Technology to develop an internet-based tool that displays state agency budget and cash balance information;

- providing five percent of bonding capacity of severance tax bonds for tribal infrastructure projects beginning in fiscal year 2012;

- requiring the enabling legislation for new economic development tax incentives to follow certain guidelines and requiring the Economic Development Department to publish an annual aggregate list of incentives; and

- allowing state agencies to accept payment by credit card or electronic means and allowing agencies to charge a convenience fee for those transactions.

There being no further business, the committee adjourned at 1:02 p.m.

REVENUE STABILIZATION AND
TAX POLICY COMMITTEE

Section 4

July 2010
Agenda
Minutes

Revised: July 7, 2010

TENTATIVE AGENDA
for the
SECOND MEETING IN 2010
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

July 8-9, 2010
Room 322, State Capitol
Santa Fe

<u>Thursday, July 8</u>

9:00 a.m.	**Call to Order** —Representative Edward C. Sandoval, Chair
9:05 a.m.	**Tax Expenditures — Policy for Assessing** —Thomas Pogue, Professor Emeritus of Economics, University of Iowa
10:30 a.m.	**Tax Incentive Overview** —Dorothy "Duffy" Rodriguez, Secretary-Designate of Taxation and Revenue —Marilyn Hill, Deputy Secretary, Taxation and Revenue Department (TRD) —Allen V. Maury, Acting Chief Economist, TRD —Clinton Turner, Senior Economist, TRD
11:15 a.m.	**One Percent Revaluation Fund Use** —Karen Montoya, County Assessor, Bernalillo County
12:00 noon	**Lunch**
1:15 p.m.	**TRD Duties, Organization and Review** —Dorothy "Duffy" Rodriguez, Secretary-Designate of Taxation and Revenue —Marilyn Hill, Deputy Secretary, TRD
2:45 p.m.	**Department of Transportation and State Transportation Commission** Organizational Review —Gary Giron, Secretary of Transportation —Johnny Cope, Chair, State Transportation Commission

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

<u>Friday, July 9</u>

9:00 a.m.	**Reconvene** —Representative Edward C. Sandoval, Chair
9:05 a.m.	**Tax Incentives — Perspectives on Effectiveness** —Fred Mondragon, Secretary of Economic Development
10:30 a.m.	**Department of Public Safety (DPS), Motor Transportation Division (MTD)** —Faron Segotta, Chief, New Mexico State Police Division, DPS —Lt. Colonel Mark Rowley, Director, MTD, DPS
12:00 noon	**Adjournment**

MINUTES
of the
SECOND MEETING IN 2010
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

July 8-9, 2010
Room 322, State Capitol
Santa Fe

The second meeting of the Revenue Stabilization and Tax Policy Committee (RSTP) for 2010 was called to order by Representative Edward C. Sandoval, chair, at 9:14 a.m. on July 8, 2010 in Room 322 of the State Capitol in Santa Fe.

Present
Rep. Edward C. Sandoval, Chair
Sen. John Arthur Smith, Vice Chair
Sen. Carlos R. Cisneros
Rep. Nathan P. Cote
Rep. Anna M. Crook
Sen. Dianna J. Duran
Sen. Tim Eichenberg
Rep. Keith J. Gardner (July 8)
Sen. Timothy Z. Jennings (July 8)
Sen. Timothy M. Keller
Sen. Gay G. Kernan
Rep. Ben Lujan, Speaker of the House
Sen. Howie C. Morales
Rep. Henry Kiki Saavedra
Rep. Jim R. Trujillo

Absent
Rep. Rodolpho "Rudy" S. Martinez
Sen. William E. Sharer
Rep. Thomas C. Taylor

Designees
Rep. Donald E. Bratton
Sen. Phil A. Griego
Sen. Clinton D. Harden, Jr.
Rep. Sandra D. Jeff

Rep. Ray Begaye
Sen. Mark Boitano
Rep. Zachary J. Cook
Sen. Kent L. Cravens
Rep. Miguel P. Garcia
Rep. Roberto "Bobby" J. Gonzales
Sen. Carroll H. Leavell
Rep. Antonio "Moe" Maestas
Sen. Steven P. Neville
Rep. Debbie A. Rodella
Sen. Nancy Rodriguez
Sen. Bernadette M. Sanchez
Sen. John M. Sapien

Rep. James R.J. Strickler
Rep. Don L. Tripp
Rep. Luciano "Lucky" Varela
Sen. Peter Wirth

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

<u>Thursday, July 8</u>

The minutes of the June 7, 2010 meeting of the committee were adopted without corrections.

Tax Expenditures — Policy for Assessing

Thomas Pogue, professor emeritus of economics, University of Iowa, gave the committee a presentation on methods of evaluating the effectiveness of business tax expenditures. Tax expenditures are special tax provisions in law that are designed to create incentives for certain types of business activity. They should be thought of as a type of government spending, rather than as tax policy, because they allocate tax revenues and reduce a government's budget surplus or reserves, just as appropriations do. Business tax credits and exemptions reduce the amount of total revenue collected in taxes.

Dr. Pogue said that business tax credits should have as a goal to improve the living standards of New Mexicans, which can be achieved by increasing the total value of goods and services produced in the state and the incomes New Mexicans derive from that production. However, many tax credits are defined more narrowly, such as to increase investment in manufacturing or to create high-wage technology jobs. Such narrow definitions can have negative overall effects on the state's economy because a credit granted to one segment of the economy will be paid for by other sectors, which could diminish the total value of production in the state. Dr. Pogue said that a narrowly defined credit should not be implemented without first determining how the credit and its financing will affect total production and income. Business credits should be based on identified needs for changes in resource use and based on evidence that a credit can, in fact, direct those resources to more valuable uses.

New Mexico currently has 27 business credits, all of which have been enacted since 1979 and most of which have been created in the past decade. The budgetary cost of credits has increased over time, accounting for two percent of general fund spending for fiscal year 2009. This amount is not the full cost of the credits because state agencies incur costs to oversee the implementation of the credits.

In order to evaluate the effectiveness of a business credit, it should be determined to what extent the actions subsidized by the credit would have occurred without the credit. If the same level of action would have occurred, then the credit does not serve its intended purpose and should be eliminated. Regardless of whether a credit has its intended effects, a credit has after-tax income and spending impacts, which should be measured. Taxpayers that receive the credit have increased disposable income and spending. In order to offset the revenue lost from a credit, the government must reduce spending or increase taxes on other businesses, which tends to reduce disposable income and spending in other segments of the economy. The task in evaluating a credit is to estimate the net effect of these changes in spending flows. A credit is cost effective only if it diverts spending and resources from less valuable to more valuable economic activities.

There are many complications that arise when trying to evaluate tax credits, said Dr. Pogue. Most credits do not require sufficient reporting in order to evaluate their effectiveness. Data needed include state government revenue foregone; what recipient businesses are doing differently because of the credit; state agency compliance and administrative costs; the extent to which the credit benefits out-of-state businesses and individuals; the net effect of the multiplier effect of a credit, which measures increased tax revenue from increased productivity against decreased tax revenue from cuts in other areas in government spending; the effect of the credit on employment, taking into account net job changes, rather than merely new jobs created in a particular industry or by a particular business; the effect of the credit on wages; and the overall effects from multiple government subsidies on a business that receives a credit.

Dr. Pogue said that, typically, it is impossible to determine definitively whether a tax credit will have a positive economic effect. The best that policymakers can do is to set out clear guidelines for credits in order to increase the likelihood that credits will be cost effective. He presented a list of guidelines that policymakers could establish, including the following:

- Establish the need for the credit. Why is there a need for an incentive to shift resources? Does the credit duplicate existing incentives? The strongest case for the establishment of a credit is to offset recognized market failures in which businesses are unwilling to perform the identified activity due to high risk, failure to account for external benefits and limited knowledge of new technologies.

- Set measurable goals. Goals of the credits should be stated in terms that are measurable.

- Offset revenue loss. The full cost of a credit should be established and budgeted before it is enacted. Any claim that a credit's costs will be offset by expanded economic activity should be supported by a quantitative analysis of that claim.

- Certification. Some credits that involve technologically complicated activities may need to have certification of the credit by a state agency before it can be claimed.

- Refundable or carry-forward credits. A credit should be fully refundable or be allowed to carry forward in future tax years if it is actually effective in directing resources to more valuable uses. If an effective credit is allowed to be taken only against tax liabilities, then businesses without those liabilities may be unwilling to change their activities. That restriction can limit the extent to which the credit is used, which may defeat the purpose of the credit.

- Recapture. Businesses that do not fulfill the requirements of a credit may have the credit revoked, and the previous credit granted can be recaptured. However, the possibility of recapture may make businesses reluctant to apply for the credit if the outcome of the change in activity is uncertain for that business. Recapture is appropriate when events subsequent to payment of the credit prevent it from having its intended effect. For example, a new jobs credit should be recaptured if a business ceases operation for an extended time after the granting of the credit. One method of avoiding recapture issues would be for the state to grant a credit on a post-performance basis.

- Transferability. Transferable tax credits are not cost effective for the state in providing incentives for certain types of business activities. Refundable credits are more cost effective.

- Limits on overlap, outlays and duration. Policymakers should decide to what extent a business should be allowed to receive multiple subsidies for performing the same business activity. The state should also determine whether a certain dollar amount of credit needs to be established and whether the credit should terminate after a certain time.

- State agency oversight and reporting. The state agency that oversees a credit should be required to report on the cost effectiveness of the credit. Evaluations should not solely rely on information provided by credit recipients.

- Taxpayer reporting requirements. Businesses that receive a credit should be required to report periodically on specified information so that the state can measure whether the credit is cost effective. Businesses should also report on every state and local incentive they receive from various programs in order to accurately measure the effectiveness of the credit being analyzed.

Representative Sandoval asked Jim O'Neill, tax consultant, to comment on tax expenditure policy. Mr. O'Neill said that unless statutes protecting confidentiality are modified, it will be difficult to get more reporting information from businesses on existing tax credits. He suggested that any new credit require full disclosure from the receiving entity as a condition of being granted the credit. Mr. O'Neill also suggested that a single system of taking credits against combined reporting system (CRS) taxes should be established, which would make administration of credits more streamlined. Finally, he said that the state pays twice for some credits because of the municipal credit against the gross receipts tax (GRT).

Questions and comments from committee members included the following:

- Are some businesses double-dipping with tax credits? Mr. O'Neill said that many businesses receive two or even three types of subsidy for a single activity.

- How does competition with other states factor into the establishment of business tax credits? Dr. Pogue said that interstate competition is often the political factor that determines whether a tax credit is enacted. However, nationally, interstate competition is a zero-sum game or even worse if one accounts for the amount of money spent by each state's economic development department. He said that many studies have shown that, in reality, a state tax burden tends to be on the bottom of a business' list of priorities in contemplating relocating. More important than tax policy is access to transportation, capital availability, the presence of an educated labor force and access to raw materials.

- Tax exemptions are not reported, so the full cost of exemptions is not fully known. Mr. O'Neill said that if current GRT exemptions were changed into deductions, businesses would be required to report those deductions. The state could then determine the amount of tax expenditures for those entities.

- Industrial revenue bonds issued to attract certain businesses to a city merely shift the property tax burden to other entities in the region.

- What new tax credits could be enacted that would help New Mexico's small businesses to stay afloat? Dr. Pogue said that taxes are a small part of a business' costs, so the state does not have much leverage over profitability. Mr. O'Neill suggested that a tax credit based on a business' payroll would stimulate job creation and help businesses.

- Usually a tax credit is paid for by some other tax increase elsewhere. Large corporations tend to get most of the business tax credits in New Mexico.

- How significant is the economic multiplier effect for a business tax credit? Mr. O'Neill said that anyone claiming a multiplier effect of greater than two is probably wrong. Dr. Pogue said that a factor of 1.2 is more common, if there is any net positive economic impact at all.

- How can the state leverage better access to capital for businesses? Dr. Pogue said that with the current tight capital markets, the state providing investment support could be a significant help to New Mexico's businesses.

- The burden of tax credit reporting should be placed on the recipients of credits, rather than the state. Dr. Pogue agreed and suggested that businesses could be charged an administrative fee for the state's oversight duties.

Tax Incentive Review

Duffy Rodriguez, secretary-designate of taxation and revenue, Marilyn Hill, deputy secretary, Taxation and Revenue Department (TRD), and Clinton Turner, senior economist, TRD, updated the committee on business incentive tax credits that the department administers. Secretary-Designate Rodriguez agreed with comments made by Dr. Pogue, adding that tax expenditures should not be evaluated using tax policy principles but should be evaluated using the same expenditure principles that are used to evaluate other expenditure programs. Consideration must be given to the intended purpose of the tax expenditure, to other types of business subsidies that may be combined with a tax credit and to quantitative analyses that evaluate the effectiveness of a tax expenditure.

Mr. Turner presented fiscal year 2010 tax expenditure estimates for the state's business credits. The total value of credits for fiscal year 2010 is estimated to be $94.3 million, which is down from last year's total of $122.7 million. The film production tax credit is still the state's largest credit, accounting for $65 million. The credit cost the state $76.7 million in fiscal year 2009. The high-wage jobs tax credit, which cost $14.4 million in fiscal year 2009, fell to $4.9 million in fiscal year 2010. In a similar reflection of the state's economic condition, the investment credit, which is a credit for certain industrial capital asset acquisitions, fell from $11.6 million to $5.9 million. Secretary-Designate Rodriguez said that she would like to present personal income tax credit data to the committee later in the interim.

Questions and comments from committee members included the following:

- The TRD was asked to provide tax credit information about companies receiving the credit. Mr. Turner said that confidentiality statutes prohibit the department from providing taxpayer information, unless a particular payment in excess of $10,000 is made to an entity. He said that the TRD could easily provide a list of credits granted and sorted by industry groups.

- The rural health care practitioner tax credit is the most important tool in recruiting health care providers to many parts of the state. Secretary-Designate Rodriguez said that most business tax credits were enacted to achieve a public policy goal rather than an economic development goal.

- Is there a time limit for companies to claim the film production tax credit? Mr. Turner said that there is not, but there is no incentive for companies to delay the submission of the fully refundable credit.

- What are the reporting requirements for business tax credits? Mr. Turner said that before a credit is granted, an applicant must submit a detailed application. Each credit has different reporting requirements after a credit is granted, however.

- More than two-thirds of the state's entire business tax credits go to the film industry. In addition, the state has loaned $240 million, interest free, to film companies over the past several years.

- The department was asked to provide more information about the effectiveness of the research and development small business tax credit, which has fallen from $249,000 claimed in 2007 to $20,000 in 2010.

One Percent Revaluation Fund Use

Karen Montoya, Bernalillo County assessor, presented to the committee proposed legislation that would allow counties to use excess money in their county property valuation funds to partially offset future mill rate increases. The fund was set up in each county to provide assessment tools for counties to better manage appraisals. Administrative charges of one percent of property tax received by counties are deposited in the fund. Currently, Bernalillo County has an excess of money in its fund, but it has no statutory authority to use that money for other purposes. Ms. Montoya proposed that Section 7-38-38.1 NMSA 1978 be amended to allow unneeded money to be used to offset the property tax mill rate the following year. She estimated that in Bernalillo County, an average household property tax bill could be reduced by $50.00 if the changes were enacted into law.

A committee member suggested that the wording in the proposal be modified to require, rather than allow, the county assessor to use the excess money in the fund for property tax relief.

TRD Duties, Organization and Review

Secretary-Designate Rodriguez presented information to the committee about the structure and duties of the TRD. The department consists of seven divisions, including the Motor Vehicle Division (MVD), Property Tax Division, Revenue Processing Division, Audit and Compliance Division (ACD), Tax Fraud Investigations Division, Information Technology Division and Administrative Services Division. In addition, the office of the secretary consists of the tax policy office, ombudsman, legal services, administrative hearing office and public information officer. The department collects and distributes taxes, distributing $5.7 billion in various taxes in fiscal year 2010. GRTs account for 64 percent of distributed revenues, followed by oil and gas revenues at 15 percent; personal income tax at six percent; fuel taxes at five percent; motor vehicle excise tax at four percent; and corporate income tax, gaming tax, weight distance tax (WDT) and cigarette tax each at one percent. Various other taxes make up the remaining two percent of revenues distributed by the department. The department's budget has seen a steady increase in the past several fiscal years, reaching a total operational budget in fiscal year 2010 of $90 million. The department's budget was cut, however, in fiscal year 2011 to $84 million. The department has a total of 1,183 authorized full-time-equivalent positions (FTEs), with vacancies in 180 positions.

The TRD is developing several technological improvements that will save the state money and provide better services to its customers. The department continues to implement its electronic filing initiative and will soon begin requiring electronic filing by certain large taxpayers. The MVD web site is being redesigned, and the department's call center system is being replaced with a much more efficient system. Finally, the department's entire web site is being redesigned, which will make it easier for taxpayers to find information and file returns.

Secretary-Designate Rodriguez updated the committee on the department's Fair Share Initiative, which was begun in 2009 to collect additional delinquent taxes. The program has $5.1 million in recurring costs, but it was expected to raise $29.2 million in fiscal year 2010 and $44.4 million in the current fiscal year. However, due to the fiscal year 2010 budget cuts and the reductions in tax revenues due to the economic recession, the Fair Share Initiative is expected to only raise $25.9 million for fiscal year 2010.

The ACD is improving its auditing functions by adding more data sources to the data warehouse to enable it to easily identify taxpayer discrepancies. It also uses a scoring system to rank potential candidates for auditing and compares 1099 forms issued by the Department of Finance and Administration (DFA) to reported income. The division expects to conduct 770 field audits, 791 managed audits, 49 desk audits and 130 business credit audits in fiscal year 2010.

The TRD also collects revenues for the WDT and trip tax. Revenues from the taxes reached a high of nearly $100 million in fiscal year 2007, but they have dropped each year since. Fiscal year 2010 revenues are expected to be $80 million. The ACD has set up a special unit dedicated to processing WDT returns and providing taxpayer assistance to the trucking industry. The division also has a WDT audit unit that performs an average of 65 WDT audits annually. The department works with the Motor Transportation Division (MTD) of the Department of Public Safety (DPS) in ensuring WDT and trip tax compliance. The MTD operates electronic license plate readers at various state ports of entry and has two mobile readers for intrastate compliance efforts. The MTD also has conducted WDT enforcement operations in the Albuquerque-Santa Fe area. The TRD data warehouse collects information on MTD compliance, and the system automatically compares its data with third-party data to identify tax deficiencies.

The Tax Fraud Investigations Division enforces the criminal statutes relative to the Tax Administration Act. It identifies and prosecutes fraud, while encouraging voluntary compliance with tax laws. The division also conducts internal auditing within the TRD to ensure the department's accountability and effectiveness. In fiscal year 2010, 21 criminal investigations were initiated and seven criminal convictions were obtained. The division also completed 16 internal audits and 16 internal investigations.

The MVD is responsible for assuring compliance with the Motor Vehicle Code. Its duties include licensing commercial and non-commercial drivers; issuing registrations, titles and licenses for vehicles; licensing auto dealers and title service companies; and contracting with private entities to provide selected MVD services. The department is developing a new "Drive MVD" system that will make MVD services easier to access. Customers will be able to make appointments online, rather than waiting for hours at a local office. Beginning in August, private MVD contractors will be able to conduct driving tests. More private retail locations have been added in Albuquerque and other cities. In fiscal year 2010, $318 million in MVD-related fees were distributed, more than 50 percent of which went to the State Road Fund (SRF). Thirty-one percent of MVD distributions went to the general fund; nine percent were distributed to local governments; the Administrative Office of the Courts received two percent; and the TRD received 4.6 percent for administrative expenses.

The Property Tax Division oversees the implementation of ad valorem taxation in each county. Property taxes contribute approximately $1.2 billion in revenues, making it the second- largest tax revenue program in the state. The division has supervisory authority over and provides technical support to county assessors. The division's budget normally consists of general fund appropriations supplemented by money distributed to it from penalties and interest. For fiscal year 2011, however, the entire division budget was appropriated from internal funds. The division's current budget is $3.3 million. The division has three bureaus: the State Assessed Properties Bureau, which assesses certain classes of property, including telecommunications, railroads, electrical utilities and oil and gas pipelines and refineries; the Delinquent Property Tax Bureau, which pursues collection of delinquent taxes and as a last resort conducts public auctions to sell delinquent property; and the Appraisal Bureau, which provides assistance to counties in the assessment of certain types of property and reviews appraisals for the State Board of Finance.

Questions and comments from committee members included the following:

- When will the implementation of the recently enacted law allowing online renewal of driver's licenses begin? Michael Sandoval, director, MVD, said that the new system will begin in June 2011.

- Will the TRD begin automatically deducting CRS payments from taxpayers' bank accounts? Ms. Hill said that taxpayers have the option of sending a check to the department or authorizing electronic payment.

- What is the status of state implementation of the federal REAL ID Act of 2005? Mr. Sandoval said that the state was granted an extension until May 2011 by the federal government to implement the act.

- Some DWI offenders who were convicted and mandated by a judge to obtain an ignition interlock device did so, but they were not aware that they also had to obtain an ignition interlock license from the department. After having the device installed in their vehicles for the specified time, they were informed by the MVD that they still had to obtain an ignition interlock license because they had neglected to do so.

- The tax amnesty letter that the TRD recently sent to taxpayers has an intimidating tone. Phil Salazar, director, ACD, said that the division sent out different types of letters to taxpayers, depending on the type of possible violation. The letter referred to by the legislator was directed toward individuals who had already been identified as candidates for auditing. Instead of going ahead with the audit, the TRD offered those individuals to enter into the tax amnesty program.

- Since New Mexico has been licensing undocumented foreign nationals, the uninsured motorist rate in the state has dropped significantly. However, insurance companies have not cut their premiums for uninsured motorist coverage. It is not fair that some national and local politicians blame Mexico for all of the problems in the United States. Mr. Sandoval said that in 2003, 20 percent of drivers in the state were not insured. By 2010, that figure dropped to nine percent. Since 2003, 80,000 driver's licenses have been issued to persons without a social security number.

- The state should require a CRS number for all potential contract bidding.

- Any mistakes made by the TRD in estimating revenues in the next six months will have serious negative consequences for the state.

- Seventy percent of federal stimulus contracts have gone to out-of-state contractors. Is there a discrepancy between the contracts awarded and the amount of GRT collected by the department?

- The GRT is collected essentially on the honor system, and 154 auditors working for the department are not sufficient to ensure adequate compliance. Mr. Salazar said that the department audits 30 different tax programs, but that the CRS system (which includes the GRT) is the primary audit function. More than one-half of the TRD auditors work on the CRS system.

- If the legislature changed state law about licensing foreign nationals to remove language that says "regardless of immigration status", the state would be in compliance with the federal REAL ID Act of 2005. Mr. Sandoval said that the language change is an option for the state to consider. Another possible approach to licensing noncitizens or citizens who want to produce more minimal documentation than is required for a REAL ID license is to provide a second type of driver's license so that the driver remains in the state system and is required to obtain car insurance.

Department of Transportation (DOT) and State Transportation Commission (STC) Organizational Review

Secretary of Transportation Gary Giron and many members of the DOT's executive staff presented to the committee the organizational structure and operations and budget of the department. Daniel Opperman, DOT chief counsel, reviewed the powers and duties of the department and commission. The STC is created in Article 5, Section 14 of the Constitution of New Mexico, and power to determine all matters of policy for the department are granted to the commission. The STC is composed of six commissioners appointed by the governor. The commission is granted in statute the authority to control all roads designated as state highways, and much of the power of the commission is vested in the department to carry out the policies of the commission. Commission members may receive per diem and mileage, but they do not receive any other compensation or have DOT staff or offices. Each year, the department's budget is first reviewed by the commission before it is submitted to the DFA and legislature.

Secretary Giron described the organizational structure of the DOT. He said that due to the recent recession and cuts to government spending, he has reduced the number of deputy secretaries from three to two and reduced FTEs by 250 positions. The department consists of a general office and six district offices. The department has 2,500 employees and has a yearly operating budget in fiscal year 2011 of $803 million. The department is responsible for the construction and maintenance of more than 30,000 lane-miles of highway infrastructure. In the operations and maintenance program, more than 1,600 employees work at the six district offices. There are 46 construction crews and 82 maintenance patrols statewide. The programs and infrastructure component of the DOT manages several programs, including the Office of Infrastructure, program management, engineering support, the Aviation Division, the Planning Division, transit and rail, traffic safety and property asset management.

The DOT receives no general fund support, being funded entirely by the SRF and federal funds. However, the recent economic downturn led to a reduction in SRF revenues of more than $120 million in the past three years. With funding for Governor Richardson's Investment Partnership (GRIP) and federal American Recovery and Reinvestment Act of 2009 (ARRA) projects ending soon, the state's highway capital program will continue to decline at current projected funding levels, said Secretary Giron.

Deputy Secretary of Construction Programs Max Valerio described trends in the DOT's construction funding. The federal highway construction funding authorization expired in September 2009, with no reauthorization date in sight. That leaves an annual average federal funding amount of $330 million, which is further reduced by $122 million in debt service for prior projects and $60 million for various research programs and DWI penalties imposed by the federal government. GRIP funding has a $425 million shortfall, which has been partially offset by one-time ARRA funding of $135 million. Total ARRA funding for highway projects in New Mexico amounts to $252 million. Mr. Valerio contrasted fiscal year 2010 total DOT construction funding of $524 million to fiscal year 2012's expected budget of $142 million.

Deputy Secretary of Operations Domingo Sanchez reviewed forecasted distributions to the SRF from various road-related taxes and fees, including the gasoline tax, special fuel excise tax, petroleum products loading fee, WDT, trip tax, vehicle registration fees, transaction fees and driver's license fees. SRF revenue is expected to grow slowly in the next two fiscal years from $353 million to $371 million. However, distributions to the fund have dropped each year since fiscal year 2008 from a previous high of $399 million. The DOT has taken several actions to deal with reduced SRF revenue, including reducing the rollover of budgeted encumbrances; convening strategic planning sessions with district engineers to implement budget reductions; engaging in employee outreach to seek cost savings; reducing authorized FTEs by 250 positions; resolving critical issues with the SHARE accounting system for federal reimbursements; and continuing to research options for SRF revenue enhancements. The impacts of budget reductions have been felt in all areas of the department's operations: state-funded highway construction projects have been essentially eliminated in fiscal years 2009 and 2010; contract maintenance programs were cut by $21 million; heavy equipment replacement schedules for more than 80 patrols were delayed; the department reduced the purchase of field supplies, which resulted in increased deferred maintenance problems; and the department is maintaining a 19 percent vacancy rate.

Department analysis shows an annual gap in funding for routine maintenance of almost $200 million. An additional $50 million is needed each year for bridge replacement and repair. The current budget outlook only exacerbates these ongoing problems. If new funding sources are not found soon, some state highways will fall into disrepair, said Secretary Giron. He then discussed potential revenue enhancements from various tax and fee hikes to be dedicated to the SRF. For each one-cent increase in the gasoline tax, the SRF would generate an additional $8.3 million. Raising the special fuel excise tax generates $4.3 million for each one-cent increase per gallon. For each $10.00 increase in motor vehicle registration fees, the fund stands to gain $15 million annually. Secretary Giron said that he is not proposing any tax hikes yet. He pointed out a recent study, however, that ranked New Mexico's gas tax as the eighth lowest in the nation.

Questions and comments from committee members included the following:

- Is the rubberized asphalt program cost effective? Ernest Archuleta, DOT operations manager, said that one million tires from New Mexico are processed each year into polymerized asphalt. The cost of that asphalt is about 30 percent higher than standard materials, and it is still unclear whether the rubberized asphalt lasts longer than standard asphalt mixtures.

- Are there any state highways that have dangerous conditions due to lack of maintenance activities? Gary Shubert, District 2 engineer, said that no roads are currently in a dangerous condition, but if New Mexico experiences another wet winter, the district may be forced to install warning signs indicating unmaintained roads.

- Does the department save much money in closing down highway rest areas? Secretary Giron said that the DOT has plans to close 13 rest areas. The maintenance budget has already been cut dramatically, so other areas need to be trimmed before further cuts in maintenance are made.

- Will STC members lobby the next governor to provide a stable revenue source for the SRF? Roman Maes, STC commissioner, said that they will. There needs to be an increase in road taxes in order to keep roads maintained, he said.

- Increasing motor vehicle registration fees is probably politically easier than raising the gasoline tax.

- The department should avoid cutting the budget for snow removal operations.

The committee recessed at 5:10 p.m.

<u>Friday, July 9</u>

The committee was reconvened by Representative Sandoval at 9:11 a.m.

Tax Incentives — Perspective on Effectiveness

Fred Mondragon, secretary of economic development, and Lisa Strout, director, New Mexico Film Office, Economic Development Department (EDD), presented to the committee their perspectives on the importance and effectiveness of business tax incentives. Secretary Mondragon identified the most important business incentives New Mexico has. Ms. Strout subsequently discussed film incentives. Secretary Mondragon said that the EDD conducted a survey of businesses to determine which business incentives are the most effective. Solar energy incentives are definitely an area in which New Mexico "gets it", he said. The state does not create jobs; the private sector does. Financing is still very tight for companies to start up or expand. New Mexico cannot compete with China for solar energy start-up companies. If New Mexico loses any incentives in the solar energy sector, it will be almost impossible to attract new business in the state.

Secretary Mondragon said that the high-wage jobs tax credit has been a great incentive for businesses to create high-paying jobs. That credit is the best method for the state to keep the younger generation of workers living in New Mexico. The investment credit, which can be applied toward the purchase of certain manufacturing equipment, provides a more level playing field with other states, because New Mexico is one of a few states that charges a sales tax on manufacturing equipment. Small business tax credits are important, because they help small businesses get started. The rural job tax credit provides incentives for companies to locate in rural areas of the state. New Mexico primarily competes with Texas, Colorado, Utah, Arizona and Nevada for business incentives, said Secretary Mondragon. Arizona recently developed enterprise zones, and New Mexico should consider them as well. Colorado has a high-wage jobs incentive; Utah has a post-performance tax credit of up to 30 percent against all taxes and has an industrial assistance fund; and Texas has no income tax, which has cost New Mexico a few business relocation deals in the past year.

Secretary Mondragon discussed an economic impact analysis of a solar manufacturing company that located in Albuquerque. The total value of the state and local incentives granted the company is $7.4 million. The company is expected to create 855 direct and indirect jobs with a $300 million payroll over 10 years. State and local taxing districts should expect to realize $140 million in additional revenue, while only incurring an additional $7 million in costs.

Ms. Strout discussed film incentives in New Mexico. The film industry in New Mexico creates jobs in hotels, restaurants, lumber yards, etc. She said that the data being reported by the film industry in how it spends money on a film project will help the department measure the economic impact of the industry. In New Mexico, the private sector has invested heavily in the film industry all over the state. There are many companies in Santa Fe and Albuquerque serving the industry.

New Mexico offers a film production tax credit of 25 percent of film-related expenditures. In fiscal year 2009, $80 million in tax credits was claimed, and in fiscal year 2010, $65 million was claimed. Ms. Strout said that claims for the credit will probably amount to even less money in the current fiscal year. The state is in heavy competition with other states to attract film projects. Twenty other states now have film incentives that exceed New Mexico's. However, New Mexico still has much to offer that other states do not have.

In order to maximize the revenue that the state receives from the film industry, the EDD is proposing three law changes in the upcoming legislative session. The first proposal would be to enact mandatory income tax withholding provisions for performing artists. The second proposal would require that vendors of film companies have an actual physical presence in New Mexico in order for those expenditures to qualify for the tax credit. The third proposal would require that companies apply for the tax credit within one year of completion of a project's expenditures.

Questions and comments from committee members included the following:

- Does the film production tax credit include expenditures for television productions? Ms. Strout said that it does. She said the television series *Breaking Bad* has been filmed in the state for four years, which has kept many New Mexicans employed.

- Does the film production tax credit actually create more revenue for the state? Ms. Strout said that according to the 2008 Ernst & Young study of the film industry in New Mexico, for every dollar the state spends on film incentives, the state collects $1.50 in associated revenues.

- Are enterprise zones a useful economic development tool? Secretary Mondragon said that the state has two enterprise zones, but they are not currently being developed. The state does not have any special tax benefits, but the federal government does.

- With so many states competing with each other by offering economic development incentives, are they collectively engaged in a race to the bottom? Secretary Mondragon said that the state is not trying to attract minimum wage jobs, but it is going after high-paying industries. He cited examples of Fidelity, Hewlett-Packard and several solar manufacturing companies.

- How many direct and indirect jobs are associated with the state's film industry? Ms. Strout said that there are currently 3,000 people directly employed by the film industry, which translates to about 10,000 total jobs associated with the industry.

- How effective is the EDD's assistance to small businesses? Secretary Mondragon said that most tax incentives currently in law apply to small businesses. However, he said that few businesses from rural communities seek assistance from the department.

- Why does the EDD keep information about companies using tax incentives confidential? Secretary Mondragon said that many businesses that are considering relocation to the state do not want their competitors to know what they are planning.

- The state spends much money on the film industry, but the nature of that business is temporary compared to other industries. Does the EDD have any incentives for the mining industry? Secretary Mondragon said that there are infrastructure incentives, but the state cannot currently help finance equipment purchases. He said that this is an area in which the state could provide assistance in the future.

- Many regulations have been promulgated by executive order, rather than being developed by the legislature. Many of these regulations make it harder for small businesses to operate and create disincentives for businesses to locate in the state. Secretary Mondragon said that the EDD tries to work with regulatory agencies in making it easier for businesses to understand and comply with the rules.

- Has the EDD identified any areas in which it can cut operating costs? Secretary Mondragon said that he is considering merging a few divisions in the department and has identified more positions that could be eliminated. He said that the department has already lost staff from the recent budget-cutting legislative sessions. He also said that the department is restricting travel for employees and is holding more electronic meetings.

- Any business incentives should be used to attract long-term instead of short-term business investment. Business incentives should not be treated as an entitlement, which is how the film production tax credit seems to be viewed by the film industry.

- Why do businesses locate in New Mexico? Secretary Mondragon said that although business incentives are not the most important reason for companies to locate in the state, the lack of incentives can keep a company from moving to New Mexico. The main attractions New Mexico has for businesses are the quality of life, the low cost of doing business, the relatively lower cost of labor, the lower cost of real estate and the business-friendly political leadership of state government.

Motor Transportation Division of the Department of Public Safety

Lieutenant Colonel Mark Rowley, director, MTD, DPS, and Faron Segotta, chief, New Mexico State Police, DPS, presented an overview of the MTD to the committee. Motor transportation police have been in existence in New Mexico since 1938, said Lt. Col. Rowley. MTD responsibilities include law enforcement services; safety inspections on commercial motor vehicles; preventive radiological nuclear detection and response; compliance reviews and safety audits of motor carriers; motor carrier educational workshops; size and weight enforcement; and tax and permitting compliance. There are 16 ports of entry in operation, although some of them do not operate continuously. The MTD has eight regional districts, with 156 authorized police officers, 84 transportation inspectors and 33 support personnel. The division currently has 46 vacancies. Due to the economic downturn and shortfall in state revenues, the division has frozen 19 FTE positions this fiscal year. In fiscal year 2009, the division budgeted 15.5 additional FTEs, and 10.5 of those positions have been filled. The division is funded by the general fund and the SRF and is budgeted for $16 million in fiscal year 2011. The MTD general fund appropriation has been cut more than 11 percent since fiscal year 2009, and the SRF appropriation has been cut less than one percent. The MTD has received special funding in fiscal year 2011 to increase deployment of license plate readers, which will increase the enforcement capacity of the division and collect more revenue. This year, the division will install the readers at the San Jon, Raton and Lordsburg ports of entry.

Lt. Col. Rowley suggested several changes in statute to increase revenue and streamline MTD operations, including the following:

- Eliminate the Weight Distance Tax Act

In order to maximize road fund revenue, Lt. Col. Rowley recommended exploring the possibility of eliminating the Weight Distance Tax Act and replacing it with a new heavy-vehicle revenue stabilizing registration plan. Forty-six states currently use a heavy-vehicle registration system in lieu of weight distance. Implementation of a heavy-vehicle registration system would eliminate the problem of zero filers, non-filers, underreporting mileage, underreporting weight and the need to conduct audits on motor carriers to ensure compliance with the Weight Distance Tax Act. Fewer personnel would be required to administer this program. This plan was previously recommended by the MTD in 2002, 2005 and 2007.

- Issuance of Civil Assessments by Transportation Inspector Personnel

Transportation inspectors are not certified commissioned law enforcement officers and cannot issue criminal citations. Consequently, when conducting commercial motor vehicle safety inspections, weighing trucks and checking for road use tax compliance, transportation inspectors cannot issue citations and are authorized only to note those violations on the inspection reports. If a law enforcement officer is not present to issue citations, which is now more common due to a current vacancy factor of 20.5 percent for commissioned officers, these violators are not fined, resulting in lost revenue to the state.

Lt. Col. Rowley recommended that the legislature explore the possibility of allowing transportation inspectors to issue civil assessments for driver out-of-service violations, such as log book violations, medical card violations, etc.; vehicle out-of-service violations, such as brake, tire, suspension, frame and other equipment violations; overweight/oversize violations; and road use tax violations. During fiscal year 2009, commissioned police officers conducted 74,225 safety inspections and transportation inspectors conducted 40,403 safety inspections. A conservative estimate of potential annual revenue to be realized from the issuance of civilian citations by transportation inspectors is $1.1 million. This plan was previously recommended in 2002.

- Increase Fees for Multiple Trip Permits

Lt. Col. Rowley said that multiple trip permits allow commercial motor carriers to make an unlimited number of trips hauling the same commodity for one year by purchasing one permit per year per envelope vehicle. The maximum dimensions for an envelope vehicle is 140,000 pounds weight, 14-foot width, 15-foot height, 90-foot length, 15-foot front overhang and 25-foot rear overhang. The current fee for a multiple permit is $250, which is significantly lower than other states. This permit is a bargain for commercial motor carriers that make numerous oversize/overweight trips per year hauling the same type of commodity.

Lt. Col. Rowley recommended that the annual fee for a multiple trip permit be increased from $250 to $1,000 in addition to implementing the issuance of quarterly multiple trip permits for $250 each quarter. The number of annual multiple trip permits issued during fiscal year 2010 was 4,302. At $250 per permit, this resulted in $1,075,500 in revenue. Increasing annual multiple trip permit fees to $1,000 would result in $4,302,000 in revenue for the same number of permits issued in fiscal year 2010 or an increase of $3,226,500 in additional revenue. Implementing the ability to purchase quarterly permits for $250 in addition to increasing annual multiple trip permits to $1,000 would result in projected revenue above $1,075,500 and below $4,302,000 based on fiscal year 2010 data. Additional revenue would be dependent on the number of annual versus quarterly multiple trip permits purchased.

- Increase Fees for Over-Dimensional Single Trip Permits

The base fee for an over-dimensional single trip permit is $25.00 plus $.025 per ton per mile over 86,400 pounds. Lt. Col. Rowley recommended increasing the base fee to $30.00 and charging a straight $40.00 surcharge on all vehicles weighing over 86,400 pounds, regardless of the distance traveled on New Mexico highways. Under the current tax structure, a five-axle vehicle weighing 100,000 pounds that travels 100 miles on New Mexico highways would be charged $42.00 for an over-dimensional single trip permit. Under the proposed formula, this same carrier would pay a flat $70.00 for the same permit. Additional revenue collected based on fiscal year 2010 data would be at least $162,285 using the base permit fee of $30.00 and additional undetermined revenue for vehicles weighing over 86,400 pounds.

- Abolish Self-Issue Over-Dimensional Permits

Self-issue over-dimensional permits are issued in books of 10 permits for $250 and are used primarily by the mobile home industry. Because of the potential to abuse these permits by reusing permits, failing to conduct route surveys, hitting obstacles such as bridges, etc., Lt. Col. Rowley recommended that these types of permits be abolished and motor carriers be required to purchase individual single trip permits. An undetermined amount of additional revenue will be realized due to motor carriers not being able to reuse permits, requiring the purchase of a permit for each move.

- Increase Fines for Overweight Vehicle Violations

Lt. Col. Rowley recommended increasing fines for overweight vehicle violations by 50 percent. He gave the example of a vehicle that is overweight by 5,000 pounds and that is currently assessed a fine of $206. A vehicle that is overweight by 10,000 pounds is currently assessed a fine of $906. The new fine with a 50 percent increase would be $1,359. By comparison, a vehicle overweight by 10,000 pounds is currently assessed a fine of $2,070 in Arizona, $3,800 in California and $1,206 in Colorado. Minimum estimated additional revenue is $110,000 and could be significantly higher if transportation inspectors are authorized to issue civil assessments for overweight vehicles.

- Cross-Train Transportation Inspectors to Issue Driver's Licenses

Lt. Col. Rowley recommended cross-training transportation inspectors to issue driver's licenses at rural ports of entry. This would help alleviate some of the work load on the MVD in addition to providing a convenient opportunity for rural New Mexicans to obtain their driver's licenses. This program would not result in additional revenue to the State of New Mexico; however, it would certainly make the issuance of driver's licenses to New Mexicans more efficient and effective with reduced budgets and personnel.

- Move the Radiation Control Bureau from the Department of Environment to the DPS

The Radiation Control Bureau is responsible for regulating the sources of radioactivity and radiation under the statutory authority of the Radiation Protection Act in an effort to provide for protection against intrinsic hazards that radiation can pose to workers, the public and the environment.

The federal Nuclear Regulatory Commission (NRC) issued order EA-05-090 in 2005, requiring the implementation of enhanced radioactive materials security. This order requires that New Mexico radioactive material licensees certify that those with access to radioactive material under their licenses are sufficiently trustworthy and reliable. The NRC also issued order EA-07-305 in 2007, requiring fingerprinting and Federal Bureau of Investigation (FBI) identification and criminal history records checks on licensees authorized to possess radioactive material in quantities of concern.

Because of the potential to use radioactive materials as a means of terrorism, the security of radioactive materials has become a high priority over the past several years. Increased control over radioactive materials and the requirements for some licensees of radioactive materials to undergo fingerprinting and FBI identification and criminal history records checks suggest that the Radiation Control Bureau would be better situated in a law enforcement agency that has the resources to conduct these background investigations in addition to investigating suspicious and unusual activities involving radiological materials. The DPS is also actively involved in preventive radiological nuclear detection (PRND) initiatives in conjunction with the federal Department of Homeland Security's Domestic Nuclear Detection Office, the U.S. Department of Energy and the national laboratories. The expertise of personnel in the Radiation Control Bureau would greatly benefit these PRND initiatives.

There being no further business, the committee adjourned at 1:00 p.m.

REVENUE STABILIZATION AND
TAX POLICY COMMITTEE

Section 5

August 2010
Agenda
Minutes

Revised: August 20, 2010

TENTATIVE AGENDA
for the
THIRD MEETING IN 2010
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

August 23-24, 2010
Room 322, State Capitol

<u>Monday, August 23</u>

9:30 a.m.	**Call to Order** —Representative Edward C. Sandoval, Chair
9:35 a.m.	**Tax Incentives — Other-Than-Business Incentives** —Dorothy Rodriguez, Secretary-Designate, Taxation and Revenue Department (TRD)
10:45 a.m.	**Modified Combined Tax Liability — Definition** —Jim O'Neill, Consultant
11:15 a.m.	**Assessment of Tax Incentives** —Thomas Pogue, Professor Emeritus of Economics, University of Iowa • Biodiesel blending facility • High-wage jobs —Jim O'Neill, Consultant • Angel investment • Cultural properties preservation • Film production —Richard Anklam, Executive Director, New Mexico Tax Research Institute • Affordable housing • Business facility rehabilitation • Renewable energy production
12:00 noon	**Lunch**
1:00 p.m.	—Thomas Pogue, Professor Emeritus of Economics, University of Iowa • Investment tax credit • Laboratory partnership with small business —Jim O'Neill, Consultant

- Job mentorship
- Rural health care practitioner
- Technology jobs — basic and additional

—Richard Anklam, Executive Director, New Mexico Tax Research Institute

- Rural job
- Solar market development
- Sustainable building

3:00 p.m. **Discussion of Tax Incentive Report**

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

Tuesday, August 24

9:30 a.m. **Reconvene**
—Representative Edward C. Sandoval, Chair

9:35 a.m. **Review of Agency Operations**
—Pam Ray, Staff Attorney, Legislative Council Service
—Motor Transportation Division, Department of Public Safety

10:30 a.m. **The Gross Receipts Tax, Pyramiding and Economic Activity and Combined Reporting**
—Gerry Bradley, Research Director, New Mexico Voices for Children
—Tom Clifford, Chief Economist, Legislative Finance Committee
—Richard Anklam, Executive Director, New Mexico Tax Research Institute
—Helen Hecht, Tax Counsel, Federation of Tax Administrators

12:00 noon **Adjournment**

MINUTES
of the
THIRD MEETING IN 2010
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

August 23-24, 2010
Room 322, State Capitol
Santa Fe

The third meeting of the Revenue Stabilization and Tax Policy Committee (RSTP) for 2010 was called to order by Representative Edward C. Sandoval, chair, on August 23, 2010 at 9:45 a.m. in Room 322 of the State Capitol in Santa Fe.

Present	**Absent**
Rep. Edward C. Sandoval, Chair	Sen. Howie C. Morales
Sen. John Arthur Smith, Vice Chair	Sen. William E. Sharer
Sen. Carlos R. Cisneros (8/23)	
Rep. Nathan P. Cote	
Rep. Anna M. Crook	
Sen. Dianna J. Duran (8/23)	
Sen. Tim Eichenberg	
Rep. Keith J. Gardner	
Sen. Timothy Z. Jennings	
Sen. Timothy M. Keller	
Sen. Gay G. Kernan	
Rep. Ben Lujan, Speaker of the House	
Rep. Rodolpho "Rudy" S. Martinez	
Rep. Henry Kiki Saavedra	
Rep. Thomas C. Taylor	
Rep. Jim R. Trujillo	

Designees	
Sen. Mark Boitano	Rep. Ray Begaye
Sen. Phil A. Griego	Rep. Donald E. Bratton
	Rep. Zachary J. Cook
	Sen. Kent L. Cravens
	Rep. Miguel P. Garcia
	Rep. Roberto "Bobby" J. Gonzales
	Sen. Clinton D. Harden, Jr.
	Rep. Sandra D. Jeff
	Sen. Carroll H. Leavell
	Rep. Antonio "Moe" Maestas

Sen. Steven P. Neville
Rep. Debbie A. Rodella
Sen. Nancy Rodriguez
Sen. Bernadette M. Sanchez
Sen. John M. Sapien
Rep. James R.J. Strickler
Rep. Don L. Tripp
Rep. Luciano "Lucky" Varela
Sen. Peter Wirth

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

Staff
Pam Ray, Legislative Council Service (LCS)
Doris Faust, LCS
Ric Gaudet, LCS

Monday, August 23

Tax Incentives — Other-Than-Business Incentives

Dorothy Rodriguez, secretary-designate of taxation and revenue, and Al Maury, acting chief economist, Taxation and Revenue Department (TRD), reviewed for the committee more than 230 tax credits, exemptions and deductions found in New Mexico statutes. Secretary-Designate Rodriguez said that these tax expenditures are a substitute for direct government spending and should be evaluated on policy grounds periodically. Statutes usually do not state the purpose of tax incentives, and sometimes the TRD does not have enough information to interpret the language of an incentive. The TRD wants to establish uniform guidelines for all incentives and standard language. For example, the words "apply" and "claim" are used interchangeably in the statutes, but they often have very specific meanings, depending on whether the TRD has the authority to grant or deny an incentive.

Secretary-Designate Rodriguez recommended that Section 7-1-29.2 NMSA 1978 be repealed. That section automatically grants a credit to a taxpayer if the TRD has not granted or denied a credit within 180 days of making the application. The TRD does not always have enough time to evaluate the legitimacy of some complicated credit applications.

The TRD wants to establish model statutes governing business tax incentives. The existing credits have myriad rules regarding certification, recapture, transferability and refundability.

Questions and comments from committee members included the following:

- What type of project qualifies for the film production tax credit? Lisa Strout, director, New Mexico Film Division, Economic Development Department (EDD), said that a project generally qualifies for the credit if it is intended for commercial exploitation. Regional and national advertising qualify, but local advertising and news programs do not. The division was asked for a list of all entities and individuals receiving the credit.

● LCS staff was directed to review the tax incentive chart provided by the TRD, and committee members were requested to provide comments to staff on individual incentives.

● Why is the TRD unable to specify the amount of an individual deduction? Mr. Maury said that many deductions are reported as a group, and there is no way of determining exactly how much an individual deduction costs the state. Patricia Herrera of the TRD Tax Information Office said that there are specific line-item deductions for personal income tax (PIT) filers, but most deductions for gross receipts tax (GRT) filers are aggregated onto a single line.

● A system to individually identify all GRT deductions and exemptions needs to be established, and a tax expenditure budget should be created each year.

● Does the state ever audit tax-exempt organizations? Secretary-Designate Rodriguez said that the TRD does not, unless there is evidence warranting an audit for a specific entity.

● How does the TRD account for residual metal valuation to correctly impose extraction taxes? Secretary-Designate Rodriguez said that her staff will research that question and provide an answer.

● GRT "hold harmless" provisions designed to protect municipalities from the deduction on food items are hurting the state more and more as municipalities continue to expand GRT taxes. Clinton Turner, senior economist, TRD, said that the state froze the municipal distribution rate at January 1, 2007 levels, but Albuquerque subsequently reduced its GRT rate. The effect was that the city still gets a distribution at the 2007 level, which has a negative fiscal impact on the state.

● To what extent do taxpayers benefit from multiple overlapping incentives? Secretary-Designate Rodriguez said that overlapping tax incentives are widespread throughout the tax code. Very few incentives specify that if one credit is taken, then no other incentive can be granted for the same activity. In general, if a taxpayer qualifies for two different incentives for the same activity, then both incentives are granted.

Modified Combined Tax Liability — Definition

James O'Neill, tax consultant, recommended standardizing the definition of "modified combined tax liability" in various tax credit statutes and codifying in statute a 30-year-old TRD interpretation of how to determine the tax base against which the credit can be claimed. Many tax credit statutes allow a taxpayer to claim a credit against various combined reporting system (CRS) taxes. Mr. O'Neill suggested eliminating the ability to take a credit against six of the smaller CRS taxes, which will greatly simplify the administration of the credit but without substantially affecting the taxpayers. He suggested that those credits instead be counted only against GRT, compensating tax and withholding tax due. Tax credits would not be allowed against local option GRTs.

The TRD has allowed credit claimants to take a credit against the entirety of the specified taxes due, even though some of those taxes have specific earmarked distributions associated with them. The department then computed the distribution to those earmarked revenue streams as if the credit had been disallowed. Mr. O'Neill suggested putting into statute that interpretation of the law.

Finally, Mr, O'Neill pointed out that there are now two tax withholding acts in statute, and he clarified that claiming credits against wage withholding pursuant to Section 7-3-3 NMSA 1978 will ensure that the maximum amount available to a taxpayer will be allowed.

Assessment of Tax Incentives

Dr. Thomas Pogue, professor emeritus of economics, University of Iowa, Mr. O'Neill and Richard Anklam, executive director, New Mexico Tax Research Institute, reviewed for the committee 13 tax incentives.

<u>Biodiesel Blending Facility Tax Credit (Dr. Pogue)</u>:

- No stated purpose.
- Credit against the GRT and compensating tax of 30 percent of the cost and installation of biodiesel blending equipment.
- Not transferable or refundable.
- Precertification by the Energy, Minerals and Natural Resources Department (EMNRD).
- No reporting requirements.
- Full recapture of the credit in the first year.
- Carryforward allowed for four years.
- May overlap with the alternative energy product manufacturers tax credit.
- Overall cap of $1 million per year for all facilities.

This credit seems to encourage a more environmentally friendly energy source for use in vehicles. Thus, the tax credit is a "stand-in" for the external benefit the state desires. However, not all scientists agree that biodiesel is necessarily an improvement in energy conservation, especially if the fuel is corn-based. The $1 million annual limit on claims means there will not be a significant budgetary impact from the credit. Before policymakers consider raising the annual cap, the actual benefit derived from biodiesel should be established and the EMNRD should report on its effectiveness in developing new facilities.

Craig O'Hare from the EMNRD said that the tax credit has not been used by any entity, but there has been some interest.

A committee member suggested providing a tax credit for engine modification of vehicles for high-content biodiesel.

High-Wage Jobs Tax Credit (Dr. Pogue):

- No stated purpose.
- Credit of 10 percent of wages and benefits of employees up to $12,000 for four years.
- Credit can be taken against all CRS taxes except local option GRTs.
- Credit available for increases in employees, and employees must earn more than $40,000 annually in municipalities larger than 40,000 population or $28,000 in the rest of the state.
- Businesses must have more than 50 percent of sales outside the state or be eligible for development training assistance.
- The EDD provides an annual report of the credit's effectiveness.
- No recapture.
- Fully refundable.
- No carryforward.
- No overall annual cap.
- No control for overlap with other incentives.

Whether the credit is effective in actually increasing wages is difficult to determine. The number of high-wage jobs created by the credit cannot be determined without knowing what would have happened in the absence of the credit. Continuation of the credit should be based on a systemic review of this and related credits on New Mexico's economy as a whole. Recapture provisions should be enacted for businesses that cease operations within two years of receiving a credit. The out-of-state sales requirement is an unnecessary complication for qualifying for the credit. The credit is allowed only for new high-wage jobs; it does nothing to help businesses retain high-wage jobs.

John Clark of New Mexico Partnership said that his organization discusses the high-wage jobs tax credit every day with clients. New Mexico Partnership is a private, state-funded entity that serves as the EDD's business location agency. The tax credit is cited as the second most important reason businesses locate in the state; even more important is the Job Training Incentive Program (JTIP), which provides funding for employee training. He said that the reason out-of-state sales were put into the statute was to draw new money into the state. The state needs to export goods, he said.

Fred Mondragon, secretary of economic development, said that the high-wage jobs tax credit differentiates New Mexico from other states and has attracted many new businesses to the state.

Angel Investment Credit (Mr. O'Neill):

- No stated purpose, but appears to bridge the funding gap between an entrepreneur's own fiscal resources and venture capital funds.
- PIT credit.
- Up to $25,000 for investment by an accredited investor in a qualified business.
- EDD issues certificates of eligibility.
- Annual cap of $750,000.

- EDD reports annually.
- Nonrefundable.
- Carryforward allowed for three years.
- Credit expires in 2012.

One effect of this incentive is to lower the rate of return necessary to attract investment. If the credit is extended, the carryforward provisions should be standardized, with full balance payout in the last year. The angel investment credit should require recapture of the credit if the money invested is returned within a short period of time. This credit effectively replaces the unsuccessful venture capital investment credit, which has very complicated certification processes.

John Chavez, president, New Mexico Angels, said that the tax credit is a valuable tool for economic development. He said that individual investors are still investing in businesses, but venture capital fund investments have slowed down.

Secretary Mondragon said that the angel investment credit only applies to New Mexico start-up companies. The state has granted $790,000 in credits, which investment has been leveraged multiple times.

<u>Cultural Properties Preservation Tax Credit (Mr. O'Neill)</u>:
- Stated purpose is to encourage the restoration, rehabilitation and preservation of cultural properties.
- Nonrefundable PIT credit.
- Carryforward allowed for four years.
- Tax credit of up to 50 percent of the costs of a preservation project, with a maximum $25,000 per claim, or $50,000 if the project is in an arts and cultural district.
- Approval of plans by the Cultural Properties Review Committee and certification that the project was completed is required for issuance of the credit.

The projects are all on privately owned properties. This credit may be in conflict with the antidonation provisions of Article 9, Section 14 of the Constitution of New Mexico. There needs to be better reporting from the Cultural Properties Review Committee to gauge the credit's effectiveness. The carryforward terms should be standardized. Recapture provisions are not needed because the credit is not granted until the project is completed.

Alan Watson, chair of the Cultural Properties Review Committee, said that the tax credit performs a number of positive functions, including the preservation of important cultural properties, the use of high-skilled labor, the increased use of local materials and the revitalization of many communities. He said that the credit often magnifies the size of a restoration project.

Robyn Powell, tax credit and financial incentive manager of the Historic Preservation Division of the Cultural Affairs Department, said that the division has overseen 800 completed restoration projects, but some of those projects did not involve the tax credit.

Questions and comments from committee members included the following:

● How long does a completed project need to be maintained in order to keep the credit? Ms. Powell said that there are no recapture provisions in statute.

● Do municipalities provide any tax credits for cultural property preservation? Ms. Powell said that only the state provides a tax credit.

<u>Film Production Tax Credit (Mr. O'Neill)</u>:

- No stated purpose, but appears to promote direct production and post-production film work in New Mexico.
- Credit equals 25 percent of amounts spent in New Mexico and 20 percent if the film receives a federal new markets tax credit.
- No single film limit or overall annual cap.
- TRD certifies the credits; the New Mexico Film Division of the EDD first determines whether a film production company is eligible for the credit.
- Fully refundable credit against PIT or corporate income tax (CIT) liabilities.

In order for the credit to come close to benefiting the New Mexico economy overall, the multiplier effects from film production expenditures would have to be more than three. Competition with other states may mean that New Mexico will have to increase the tax credit to higher percentages in order to maintain the film production level. The state should require much more in-depth reporting from the New Mexico Film Division to determine whether the state is benefiting. Placing limitations on the annual amount of credit allowed may make other states' incentives more attractive.

Ms. Strout said that more than 250 businesses are working full time in the film industry in the state. The film industry is very different from other traditional industries. She estimated that the New Mexico economy has gained $1 billion in direct revenues from the film industry.

Questions and comments from committee members included the following:

● How does the state determine resident job creation? Ms. Strout said that employees must have a residence in the state and sign a declaration of residency.

● For each job created by the film industry, the state pays $30,000 in tax credits.

● The $70 million the state is expected to pay in film production tax credits is money that does not go into education or health care. There should be an annual cap of $30 million for the credit.

● The division was asked to provide a report on the number of New Mexicans that have received professional training in the film industry.

● The economic multiplier effect of three seems impossible. A factor close to 1.2 is more realistic.

● Although the film industry receives a large income tax credit, the industry pays many other kinds of taxes in the state.

● Would it be beneficial for the state to sunset all of its tax credits so the legislature can periodically review their effectiveness? Mr. O'Neill said that periodic review is a good idea; however, short sunset periods may dissuade businesses from locating in the state.

<u>Affordable Housing Tax Credit (Mr. Anklam)</u>:

- No stated purpose, but presumably to encourage affordable housing projects in counties with populations less than 100,000.
- Credit can be claimed against CRS taxes.
- Transferrable.
- Carryforward allowed for five years.
- Certification required by the New Mexico Mortgage Finance Authority.

This credit is not for economic development purposes; presumably, it is to encourage an activity not being met by the marketplace. There should be periodic reporting and evaluation of the credit to determine its effectiveness. Making the credit refundable would make the administration of the credit more efficient. The cost of administration of the credit for the amount granted (less than $75,000 in fiscal year 2010) is probably too high. The state should consider changing the credit into a grant program.

<u>Business Facility Rehabilitation Credit (Mr. Anklam)</u>:

- Purpose to stimulate the creation of new jobs and revitalize economically depressed areas within New Mexico enterprise zones.
- Credit can be claimed against PIT and CIT liabilities and is in the amount of 50 percent of the cost of restoration, rehabilitation and renovation of business facilities, not to exceed $50,000 per facility.
- No certification required.
- Carryforward of four years allowed.
- Credit has not been used.

There is no periodic evaluation of the credit to determine its effectiveness. Carryforward provisions should be standardized. Because this credit has not been used, probably due to the lack of enterprise zones in the state, the credit should be redesigned or repealed.

Renewable Energy Production Tax Credit (Mr. Anklam):

- No stated purpose, but presumably to encourage investment in renewable energy generation projects.
- Credit can be claimed against PIT and CIT liabilities.
- Credit is $.01 per kilowatt-hour (kwh) for wind and biomass electricity generation and $.01 to $.04 per kwh for solar electricity generation for a 10-year period.
- For projects before October 2007, carryforward of five years and transferability are allowed.
- New projects have a fully refundable credit.
- Certification required from the EMNRD.
- Annual cap of $5 million.
- Credit is phased out for new projects in 2018.

This credit needs periodic evaluation and reporting to determine its effectiveness. There is also a significant opportunity for overlap with other tax incentives, which makes the overall effectiveness of the credit difficult to determine.

Mr. O'Hare said that there are three clean energy tax incentives in statute. All credits have annual statutory caps, but the caps have not been reached.

Allan Sindelar, president of Positive Energy, a solar energy design and installation company, said that he supports the clean energy tax incentives, especially the solar market development tax credit, which provides a 10 percent tax credit for solar photovoltaic systems. He said that when the federal government enacted a 30 percent tax credit for those systems, it did not enact certification requirements. The state subsequently adopted a smaller parallel credit, but it enacted certification standards that have ensured better standards in the industry.

Brendon Miller, green economy manager, EDD, said that New Mexico has vertical integration potential in renewable energy, i.e., the state has university training programs, manufacturing companies and consumer demand for the products and services of the industry.

Randy Trainor of the New Mexico Homebuilders Association said that the association is currently working on Uniform Building Code changes to reflect sustainable building and energy principles.

A committee member said that after construction of renewable energy projects, very few jobs remain. These tax credits really just shift tax burdens to other industries.

Investment Tax Credit (Dr. Pogue):

- Purpose to provide favorable tax climate for manufacturing businesses and promote increased employment in New Mexico.
- Credit amount equal to rate of compensating tax multiplied by the value of qualified equipment.
- Credit cannot exceed 85 percent of combined compensating, GRT and withholding taxes in a given year.

- Additional employment requirement for each $500,000 in qualified equipment costs.
- No reporting requirement.
- No recapture.
- Refundable credit under specific conditions.
- Unlimited carryforward allowed.
- No overall annual cap.
- Credit can overlap with the alternative energy product manufacturers credit, but credit cannot be claimed if a research and development small business tax credit has been claimed.

The economic impact of the investment credit is small because only a small number of businesses claim the credit. The credit essentially offsets the GRT and compensating tax for the purchase of equipment for manufacturing businesses in an attempt to reduce the pyramiding of those taxes. The legislature should consider imposing the same recapture provisions as are contained in the alternative energy product manufacturers credit and consider limiting the overlap of the two credits. Replacement of obsolete equipment would be covered by the credit and administration of the credit would be simplified if the employment requirement were removed.

Secretary Mondragon said that the EDD strongly supports the investment credit, which provides an 85 percent offset of sales taxes on new equipment. Most states do not tax the purchase of equipment. He said the EDD is in favor of attaching employment requirements to most economic development credits.

<u>Laboratory Partnership with Small Business Tax Credit (Dr. Pogue)</u>:

- Stated purpose is to bring the technology and expertise of the national laboratories to small businesses in New Mexico to promote the economic development of the state, with an emphasis on rural areas.
- Credit against the GRT for qualified expenditures incurred by a national laboratory, not to exceed $20,000 per year per small business in a rural area and $10,000 in other areas.
- Extensive reporting requirements, including economic impact study for each small business assisted.
- No recapture.
- No carryforward allowed.
- Annual cap of $2.4 million per national laboratory.

This credit enables small amounts of assistance to many small businesses around the state. The low cost of the credit compared to the amount of assistance provided makes this credit very effective. More detail on how economic impacts are studied needs to be given in the reports.

Mariann Johnston from the Business Assistance Program at Los Alamos National Laboratory (LANL) said that the laboratory has assisted more than 1,500 New Mexico companies. The laboratory's economic impact report is reviewed by an independent third party prior to it being published. Last year, LANL claimed $1.9 million from the credit.

Jackie Kerby Moore of Sandia National Laboratories said that New Mexico is fortunate to have two national laboratories, and the assistance that Sandia gives to small businesses leverages small businesses across the state.

Secretary Mondragon said that the credit is very helpful to a broad sector of New Mexico companies, especially in rural areas.

Questions and comments from committee members included the following:

● How many jobs have been created as a result of laboratory partnership with small business tax credit? Ms. Kerby Moore said that Sandia has helped create more than 1,000 high-wage jobs with average annual salaries over $39,000.

● What is the definition of a "rural area"? Dr. Pogue said that the definition of rural area for this credit is every area of the state except Bernalillo County.

<u>Job Mentorship Tax Credit (Mr. O'Neill)</u>:

- Stated purpose to encourage New Mexico businesses to hire youths participating in career preparation education programs.
- Credit can be claimed against PIT or CIT liabilities of 50 percent of the gross wages of qualified students, with a $12,000 annual cap per business.
- TRD issues certificates to high schools operating a career preparation program.
- School principal executes certificate when a qualified student gets a job.
- Carryforward of three years allowed.
- No recapture.
- No reporting requirement.
- Only 23 claims filed in five years.

This credit does not have any direct participation by the Workforce Solutions Department (WSD) or the Public Education Department (PED), which could explain its low use rate. Carryforward provisions should be standardized.

Questions and comments from committee members included the following:

● Staff was directed to report on the types of career preparation programs that qualify for the credit.

● How does information about the credit get disseminated? Mr. O'Neill said that information apparently does not get disseminated. He suggested that the PED be put in charge of operating the program, instead of the TRD.

<u>Rural Health Care Practitioner Tax Credit (Mr. O'Neill)</u>:

- No stated purpose, but appears to subsidize medical professionals to encourage them to work in rural areas.
- Credit can be claimed against PIT liabilities up to $5,000 for doctors, dentists and certain other professionals and up to $3,000 for dental hygienists, physician assistants and certain nurse professionals who work in a designated rural health care underserved area.
- The Department of Health (DOH) determines eligibility to the TRD. Carryforward of three years allowed.

The DOH should report annually on the effectiveness of the credit. Some entity should certify the number of hours worked to claim the credit, rather than the applicant. The definition of "rural" is different from other tax credit definitions.

Questions and comments from committee members included the following:

● Most rural doctors are not self-employed. Hospitals get GRT credits and deductions, and doctors tend only to get a PIT credit for service in rural areas.

● Large corporate hospital chains cut corners, resulting in much higher Medicaid costs to the state. The legislature should consider giving rural health care practitioners larger tax credits and may wish to regulate "no-compete" clauses, which tend to drive health care practitioners away from rural areas when they stop service with a hospital chain.

<u>Technology Jobs Tax Credit (Mr. O'Neill)</u>:
- Stated purpose is to provide a favorable tax climate for technology-based companies to promote increased employment and higher wages in those fields in New Mexico.
- Basic credit can be claimed against CRS liabilities for four percent of qualified expenditures and eight percent in rural areas.
- Advanced credit can be claimed against PIT and CIT liabilities at the same rates, but payroll expenses must also be increased in order to qualify.
- The TRD determines eligibility.
- The TRD reports basic information about the use of the credit.
- Recapture if a business ceases operations within two years of receiving the credit.
- Carryforward allowed indefinitely.

Responsibility for operation of the program should probably reside with the EDD. Additional reporting on the effectiveness of the program should be mandated. What exactly constitutes a "technology-based business" should be clarified in statute. Carryforward provisions should be standardized.

Alan Alder, deputy secretary of economic development, said that the EDD would welcome the opportunity to implement the technology jobs tax credit.

<u>Rural Job Tax Credit (Mr. Anklam)</u>:

- No stated purpose, but presumably to encourage employment by those receiving JTIP funding in certain rural areas.
- Credit can be claimed against CRS, PIT and CIT liabilities in the amount of 6.25 percent of the first $16,000 of payroll for each qualifying job.
- Credit can be claimed for four years in very rural "tier-one" areas and for two years in "tier-two" areas.
- Carryforward of three years allowed.
- Transferable.
- Certification by the TRD.
- Reporting by the EDD, TRD and WSD on the effectiveness of the credit.

Periodic review of the credit's goals, outcomes and effectiveness should be performed. Population growth will reduce the applicability of the credit over time, so definitions of various rural areas should be standardized. The legislature should consider making the credit fully refundable or standardizing carryforward periods. The overlaps with other business subsidies should be thoroughly evaluated in order to understand the credit's effectiveness.

Secretary Mondragon said that the EDD would like to have standardized three-tiered definitions for rural and urban areas. Toni Balzano, administrator of the JTIP, said that the JTIP already has a three-tiered population definition.

Solar Market Development Tax Credit (Mr. Anklam):
- No stated purpose.
- Credit can be claimed against PIT liabilities for 10 percent of the cost of solar thermal or photovoltaic systems, not to exceed $9,000.
- Certification by the EMNRD.
- Carryforward of 10 years allowed.
- Annual cap of $2 million for solar thermal systems and $3 million for solar photovoltaic systems.
- Credit phased out for projects in 2018.

This credit should have periodic evaluation and reporting to determine its effectiveness. The legislature should consider establishing a standardized carryforward period, or making the credit refundable. The annual cap of $5 million makes this a low-risk credit to the general fund.

Sustainable Building Tax Credit (Mr. Anklam):
- No stated purpose. Credit can be claimed against PIT and CIT liabilities.
- Credit rates vary from $.30 to $9.00 per square foot, depending on size, type and efficiency rating.
- Carryforward allowed for seven years.
- Transferable.
- Annual caps of $5 million each for commercial and residential buildings and $1,250,000 for manufactured housing.

This credit should have periodic evaluation and reporting to determine its effectiveness. The legislature should consider establishing a standardized carryforward period or making the credit refundable. A policy question to ask is whether stricter building codes force builders to qualify for the credit.

Discussion of Tax Incentive Report

Ms. Ray discussed with committee members the upcoming report from the RSTP to the Government Restructuring Task Force (GRTF). She asked that members provide feedback to staff regarding specific restructuring proposals heard by the committee.

Questions and comments from committee members included the following:

- The RSTP will decide specific tax incentives and will make recommendations to the GRTF regarding the Motor Transportation Division (MTD) of the Department of Public Safety (DPS).

- The RSTP is not yet ready to make tax law recommendations, but it can make cost-savings recommendations to the GRTF.

- What is more important to the state: the film production tax credit or Medicaid and public schools?

- The RSTP should make specific systemic change recommendations to the GRTF.

- Formation of a subcommittee of members from the RSTP and the GRTF was suggested in order to discuss recommendations.

- The GRTF should examine the idea of sunsetting all credits in order to provide periodic review of incentives.

- Interim committees are not required to make recommendations to the GRTF, but they were requested by the New Mexico Legislative Council to do so if any come up during the interim.

- Some tax credits may not withstand constitutional scrutiny.

- The RSTP should investigate increasing distributions from the state's permanent funds.

The committee recessed at 4:58 p.m.

<u>Tuesday, August 24</u>

The committee was reconvened on Tuesday, August 24, 2010, at 9:38 a.m. by Representative Sandoval.

Review of Agency Operations

Ms. Ray and Lieutenant Colonel Mark Rowley, director, MTD, DPS, reviewed the operations and budget of the MTD. Ms. Ray began by reviewing the duties of the MTD, including providing law enforcement services; performing safety inspections on commercial motor vehicles; detecting and responding to radiological and nuclear exposure incidents; performing motor carrier compliance reviews and new entrant safety audits; providing motor carrier educational workshops; enforcing motor carrier size and weight restrictions; and enforcing compliance with motor carrier taxation and permitting. Overall, the taxes, fees and other revenues generated by MTD activity in fiscal year 2010 amounted to $9.5 million, down $1.2 million from the previous year. That revenue consisted of $6.2 million in port-of-entry revenue and $3.3 million in oversize/overweight permit revenue. The MTD also enforces compliance of the weight distance tax, which raised $72.2 million in fiscal year 2010.

The MTD has a budgeted allotment of 273 full-time-equivalent positions (FTEs), with 49 vacancies. In addition, 28 FTEs have been frozen during the recent economic downturn. The MTD fiscal year operating budget is $26.5 million, which is actually $2.2 million more than the previous fiscal year. The increase is due to a boost in federal stimulus funding and increases in other state fund revenue. The general fund budget for the MTD was reduced by $600,000 from fiscal year 2010.

Suggestions from the MTD for cost-savings and revenue enhancement include the following:

- elimination of the weight distance tax and substitution with an international registration plan for commercial motor vehicles;

- allowing civil citations to be issued by transportation inspectors;

- increasing the price for oversize/overweight single-trip permits;

- abolishing the ability for mobile home haulers to self-issue their permits;

- increasing the fines for overweight vehicle violations;

- cross-training transportation inspectors to issue driver's licenses; and

- transferring functions of the Radiation Control Bureau from the Department of Environment to the DPS.

Questions and comments from committee members included the following:

- What accounts for the large decrease in MTD-generated revenue since 2006? Lieutenant Colonel Rowley said that there has been an overall decrease in truck traffic in the past few years. In addition, the slowdown in the oil and gas industry has meant less oversize/

overweight revenue for the state. The reduction in FTEs at the MTD has also resulted in smaller revenue collections.

- Why are the data reflecting heavy commercial daily vehicle travel no longer available? Lieutenant Colonel Rowley said that the MTD no longer has a contract with a consultant who had access to Department of Transportation data.

- How would increases in commercial motor vehicle fees affect the oil and gas industry? Lieutenant Colonel Rowley said that other states charge much more for vehicle registration fees than New Mexico currently does, including the cost of the weight distance tax.

- Has the MTD imposed mileage limits for its officers? Lieutenant Colonel Rowley said that budget cuts have made it necessary to limit the number of miles driven by MTD officers to 2,500 miles per month.

- Mobile home haulers who obey the law should not be punished by the enactment of a law geared toward those few who use an oversize/overweight permit multiple times. State police officers should be trained to conduct motor vehicle identification inspections.

- Do other states have some form of weight distance tax? Lieutenant Colonel Rowley said that 46 other states have a heavy-vehicle registration system, rather than charging trucks per mile traveled. He said that the weight distance tax is essentially collected on the honor system and said that intrastate trucking companies do not like that tax.

- Does the MTD have citation quotas for its officers? Lieutenant Colonel Rowley said that the MTD does not have quotas, but it does have recommendations for expected activity of its officers. He said that the MTD issued 55,217 citations in fiscal year 2010, and 50 percent of those resulted in convictions. Many of those citations were issued as warnings rather than penalty violations. The division was asked to provide the actual conviction rate of citations, discounting warnings. Lieutenant Colonel Rowley said that state law does not allow for verbal warnings; some sort of written citation must be issued. He said that the MTD does not receive conviction data from the courts; it estimates conviction rates based on revenue received.

- Does the New Mexico State Police (NMSP) provide any assistance to the MTD? Lieutenant Colonel Rowley said that the two divisions share many resources. There was an unsuccessful effort in 2002 to train state police officers in commercial vehicle enforcement. A committee member said that because the MTD is performing many duties of the NMSP, it may have difficulty in performing its primary mission of commercial vehicle enforcement.

- Staff was directed to research the issue of the DPS canine unit being under the control of the NMSP, which sometimes causes difficulty in MTD drug interdiction efforts.

- Staff was directed to research the possibility of moving commercial transportation regulatory duties of the Public Regulation Commission to the MTD, including the regulation of school buses and intrastate motor carriers.

- Does the MTD share in revenue raised from drug confiscation efforts? Lieutenant Colonel Rowley said that drug forfeiture money first goes to the federal government, and then the MTD is eligible for a portion of the money. There are very strict rules about how that money can be spent, and the money cannot be used to support operating budgets.

- The state needs to direct more money for the operation of the MTD, which will raise more revenue for the state general fund. The division also needs its own canine unit.

- How would the transfer of functions of the Radiation Control Bureau affect the regulation of radiologist technicians, who are currently regulated by the bureau? Lieutenant Colonel Rowley said that the MTD is primarily concerned with radioactive material source security.

- Staff was asked to research how to improve the functioning of law enforcement communication systems, especially in rural areas.

Tax Incidence Models

Gerry Bradley, research director, New Mexico Voices for Children, presented a proposal to the committee recommending that the state track the tax incidence level on New Mexico households. Policymakers should know how regressive or progressive the overall tax structure is in the state. A tax incidence model would allow an objective look at the state's tax system in terms of income distribution and would allow policymakers to assess the regressivity or progressivity of proposed tax increases and decreases. Mr. Bradley also discussed how various states have implemented tax incidence models. Finally, he discussed a 2007 study by the Institute on Taxation and Economic Policy (ITEP) that showed that the poorest residents of the state pay a higher percentage of their incomes in state and local taxes than do their wealthier neighbors.

Questions and comments from committee members included the following:

- The property tax system is unfair in counties that have a high percentage of federal land. Industrial revenue bond issuance compounds the problem, because big businesses tend not to pay property taxes.

- Does New Mexico have a regressive or progressive tax structure? Mr. Bradley said that the state probably has a somewhat regressive system, but the actual tax incidence on residents needs to be studied in depth so that future tax law changes can be made with better information.

- Although the ITEP handout showed taxes paid as a percentage of personal income, it does not show the percentage of actual taxes paid by income category. The objectivity of the ITEP study was questioned. Mr. Bradley said that he would research all of the assumptions of that study and report back to committee members.

Corporate Income Tax Distortion and Cures for Distortion

Helen Hecht, tax counsel, Federation of Tax Administrators, discussed with the committee economic distortions within the CIT. A multistate corporation is taxed by each state that has a CIT according to its own apportionment formula to determine the portion of income earned by a corporation from activities within the state. While there is no one typical apportionment formula, each state's formula is designed to calculate the portion of the taxable income of a multistate corporation. Because other states are free to use a different method to determine their own shares of that income, multistate businesses can be taxed on more or less than all of their income. In New Mexico, the CIT is calculated by using the three factors of payroll, property and sales in the state compared to the company's total of those factors.

Many businesses are organized as affiliates operating as separate entities within one company. Expenses incurred by one affiliate might benefit the operations of another, which leads to difficulties in determining the right way to apportion taxable income for the business. If state CIT is imposed strictly on the taxable income of each separate legal entity, then the tax results may be artificially distorted if the separate legal entity represents only one piece of the total business operation of a corporate group. States that allow separate corporate filing, like New Mexico, have become concerned with the kind of artificial tax results that comes from certain transactions between the members of a corporate group that can affect the taxable income of each entity in the group.

The federal government generally treats such corporate groups as consolidated entities in which inter-company transactions do not affect the taxable income of the entire group. States are prohibited for constitutional reasons from requiring consolidated filing, but they can require combined filing, which works in a similar fashion. A state that requires combined filing treats an entity as part of a unitary business with other entities in the group and taxes the entire unitary business according to the apportionment formula of the state.

Ms. Hecht provided an example of how several tax results can be achieved by a business from choosing different filing methods in each state in which it does business. In the example, if the company files as a combined entity in both states, each state receives an equal portion of the tax due. If the company files as separate entities, the entity that had a profit will pay more tax to the state in which it is situated and none to the state in which the entity had a loss, plus a carryforward against future taxes. The total tax paid by the company is the same as in the separate filing method, but one state receives all of the tax. Finally, if the company chooses combined filing in the state in which there is a profit and separate filing in the state with a loss, the company ends up paying only a portion of its taxable income. The reason for that is that the company pays tax in the profitable state as if the company would be paying the rest of the tax due in the other state, but it actually claims a loss in the other state, because its separately treated entity in that state did not earn a profit. Ms. Hecht said that this choice of filing method can provide an incentive for a company to invest in certain states, depending on the circumstances.

The next example she cited used the same assumptions but dealt with a company that further divided its business by creating a separate royalty company. The parent company makes a tax-free contribution of intangible property rights, such as copyrights and trademarks, to the royalty company, which in turn charges branch companies in individual states for the use of those property rights. The royalty company pays a nontaxable dividend to the parent company, which then reinvests that money with the branch companies. The net effect is to keep the same cash at the branches, but from a tax standpoint, the branch companies suddenly have a huge expense item with which to reduce state tax liabilities. In the state with separate filing, the company would pay no tax because of the intra-company royalty charges. In the state with combined filing, the state would pay its apportioned share of tax, because only that state's total share of the company would be taxed. In effect, the royalty company would be treated as if it did not exist. This type of tax benefit is usually considered not to be an intended benefit for taxpayers by policymakers. Most state courts have sided with tax agencies in tax cases if the following facts have been shown:

- the structure or transactions that result in the tax savings have no real economic impact on the corporations involved;

- the structure is artificial, or the transactions are merely "paper" transactions between commonly controlled entities;

- the transactions are entirely intra-company and are not the kinds of transactions the company would engage in with unaffiliated third parties; and

- the sole purpose of the structure and transactions is to reduce state taxes.

States have many cures for this type of tax distortion, including requiring unitary combined reporting; requiring companies to add back certain intra-company charges and expenses; using the authority granted by the Uniform Division of Income for Tax Purposes Act (UDITPA) to add back deductions or to require combined reporting on a case-by-case basis; determining that certain companies have economic nexus within the state and taxing a portion of their income; determining that certain transactions are done solely for tax purposes and disallowing those transactions from being deducted from taxable income; and requiring that intra-company transactions be priced the same as third-party transactions.

Ms. Hecht said that although New Mexico has the authority through UDITPA to require combined reporting, this power can only be done on a case-by-case basis. Requiring combined reporting for interstate companies or providing for add-back provisions would apply more generally and would be more predictable for companies. If the state adopts combined filing, the legislature should also decide the standard to apply in determining whether a company is a unitary corporation; whether net operating losses of and tax credits granted to a separate entity will be available for use by the combined group; and how to combine entities with special apportionment rules. Add-back statutes can cure many types of distortion, but they are generally narrowly defined to catch the kind of loophole described in

Ms. Hecht's presentation. An add-back statute may have no impact on a large number of corporations doing business in New Mexico.

A committee member asked if a company can change its filing status from year to year. Ms. Hecht said that a company can choose to switch from filing as a separate entity to either combined or consolidated, but once that determination has been made, a switch back to separate filing requires permission from the secretary of taxation and revenue.

There being no further business, the committee adjourned at 12:35 p.m.

REVENUE STABILIZATION AND
TAX POLICY COMMITTEE

Section 6

September 2010
Agenda
Minutes

Revised: September 13, 2010

TENTATIVE AGENDA
for the
FOURTH MEETING IN 2010
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

September 14-15, 2010
Room 322, State Capitol

<u>Tuesday, September 14</u>

9:30 a.m. **Call to Order**
—Representative Edward C. Sandoval, Chair

9:35 a.m. **Tax Policy — Gross Receipts Tax and Pyramiding**
—Tom Clifford, Chief Economist, Legislative Finance Committee
—Richard Anklam, Executive Director, New Mexico Tax Research Institute

11:00 a.m. **Tax Incentives**
—Dorothy Rodriguez, Secretary-Designate, Taxation and Revenue Department (TRD)

12:30 p.m. **Lunch**

1:45 p.m. **TRD Review — Summary and Discussion**
—Pam Ray, Staff Attorney, Legislative Council Service (LCS)
—Dorothy Rodriguez, Secretary-Designate, TRD

3:30 p.m. **Department of Transportation Review — Summary and Discussion** —Pam Ray, Staff Attorney, LCS
—Gary Giron, Secretary, Department of Transportation

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

<u>Wednesday, September 15</u>

9:00 a.m. **Reconvene**
—Representative Edward C. Sandoval, Chair

9:05 a.m. **Permanent Funds — Source, Earnings and Distributions**
—Patrick H. Lyons, Commissioner of Public Lands
—Stephen K. Moise, State Investment Officer

11:30 a.m.	**PIT and CIT Proposals — Council on State Taxation Ranking** —James P. O'Neill, Consultant
12:00 noon	**Adjourn**

MINUTES
of the
FOURTH MEETING IN 2010
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

September 14-15, 2010
Room 322, State Capitol
Santa Fe

The fourth meeting of the Revenue Stabilization and Tax Policy Committee (RSTP) for 2010 was called to order by Representative Edward C. Sandoval, chair, on Tuesday, September 14, 2010, at 9:37 a.m. in Room 322 of the State Capitol in Santa Fe.

Present
Rep. Edward C. Sandoval, Chair
Sen. Carlos R. Cisneros
Rep. Nathan P. Cote
Rep. Anna M. Crook
Rep. Keith J. Gardner (9/14)
Sen. Timothy M. Keller
Sen. Gay G. Kernan
Rep. Ben Lujan, Speaker of the House
Rep. Rodolpho "Rudy" S. Martinez
Sen. Howie C. Morales (9/14)
Rep. Henry Kiki Saavedra
Rep. Thomas C. Taylor
Rep. Jim R. Trujillo

Absent
Sen. John Arthur Smith, Vice Chair
Sen. Dianna J. Duran
Sen. Tim Eichenberg
Sen. Timothy Z. Jennings
Sen. William E. Sharer

Designees
Sen. Mark Boitano
Sen. Phil A. Griego
Sen. Clinton D. Harden, Jr.

Rep. Ray Begaye
Rep. Donald E. Bratton
Rep. Zachary J. Cook
Sen. Kent L. Cravens
Rep. Miguel P. Garcia
Rep. Roberto "Bobby" J. Gonzales
Rep. Sandra D. Jeff
Sen. Carroll H. Leavell
Rep. Antonio "Moe" Maestas
Sen. Steven P. Neville
Rep. Debbie A. Rodella
Sen. Nancy Rodriguez
Sen. Bernadette M. Sanchez

Sen. John M. Sapien
Rep. James R.J. Strickler
Rep. Don L. Tripp
Rep. Luciano "Lucky" Varela
Sen. Peter Wirth

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

Staff
Pam Ray, Legislative Council Service (LCS)
Doris Faust, LCS
Ric Gaudet, LCS

Guests
The guest list is in the meeting file.

Handouts
Handouts and other written materials are in the meeting file.

<u>Tuesday, September 14</u>

Tax Policy — Gross Receipts Tax and Pyramiding

Richard Anklam, president and executive director, New Mexico Tax Research Institute, and Tom Clifford, chief economist, Legislative Finance Committee (LFC), gave a presentation to the committee about the gross receipts tax (GRT) and pyramiding issues associated with the tax. Mr. Anklam began by providing a general definition of "pyramiding", which is when a general consumption or transaction tax is charged on business inputs and becomes embedded as part of the cost of the ultimate goods or services sold to the consumer. For example, a construction company that buys engineering services is normally charged GRT. Part of the cost of engineering services includes accounting services for the engineering company, which also includes GRT. Part of the cost of the accounting services includes printing services on which the GRT is charged. Part of the cost of printing services includes business supplies on which the GRT is charged. Economists have argued that, ideally, the GRT should be applied only to the final consumption and not to business inputs. However, this ideal often conflicts with another tax principle: that the GRT tax base should be as broad as possible. With a broad tax base, the GRT is imposed on more goods and services purchased by businesses.

Pyramiding of sales taxes is a common problem in most states. Many states have taken steps to alleviate pyramiding in an attempt to reduce the economic distortions it causes. Pyramiding has many effects, including:

- if the sales tax rate is higher, the effects of pyramiding are much more pronounced;

- small businesses often feel the effect of pyramiding on services because they tend to purchase business services instead of having those services provided in-house;

- businesses and individuals that make in-state purchases are impacted more than those that purchase from out-of-state vendors, which creates an incentive to purchase from out-of-state vendors;

- most of the tax burden caused by pyramiding is likely borne by in-state households, which makes the tax more regressive;

- in-state companies are placed at a disadvantage compared to their out-of-state competitors; and

- the tax becomes less transparent with greater levels of pyramiding.

New Mexico has a GRT that is a business privilege tax imposed on a seller's gross receipts and has a very inclusive definition of most goods and services provided. The state GRT rate is 5.125 percent, and local governments can charge additional GRT. The average local option GRT is two percent. The state also charges the compensating tax of 5.125 percent on purchases of goods used in New Mexico that are purchased from out-of-state sellers. Services provided by out-of-state vendors are not subject to the compensating tax. The GRT and compensating tax base have several exemptions and deductions to reduce the pyramiding effect, including exemptions from wages and salaries; transactions taxed under other taxes; dividends; deductions of items sold for resale; tangible property sold to governments; food for home consumption; certain medical services; and a long list of special industry deductions.

Even with the exemptions and deductions from the GRT and compensating tax base, a substantial portion of purchases by businesses in New Mexico remain. The state has greater pyramiding effects than most other states because New Mexico taxes more service and non-service business inputs. Historically, the broad-based GRT in New Mexico made sense because the minimal role of cross-border transactions kept retail competition mostly local; the large role of government facilities and the imposition of the GRT on sellers of services to those facilities increased the tax base tremendously; and the imposition of the GRT on services for the resource extraction industry further increased the tax base. However, the relative isolation of the New Mexico economy is changing, and competitiveness with out-of-state businesses is becoming a bigger issue.

The debate surrounding the pyramiding issue is complex. Pyramiding is seen as a problem not just by economists, but also by businesses that perceive that the tax on their purchases adds to their costs, making them less competitive. In addition, sales of services are becoming a larger portion of the economy, which leads to other problems, including how to determine where the sale of a service takes place and when a service becomes an input of another subsequent service. Although many business inputs are allowed a deduction if they are to be resold, many inputs are still taxable.

Because one-third to one-half of GRT revenue comes from pyramiding, the problem will be expensive to address. In 2003, the Blue Ribbon Tax Reform Commission recommended fixing the deduction allowed for items and services for resale, but the solution had a $50 million annual cost to state coffers. Any solution to the problem should not involve raising GRT rates because that will compound the inefficiency of the tax and increase its regressivity. The use of tax incentives should be strictly limited because they reduce the base and put upward pressure on tax rates. In general, GRT reform should focus on taxing final sales and exclude intermediate sales. Specific deductions should be made for business inputs. The GRT could also be split into two taxes: a retail sales tax on consumption and a business privilege tax.

Mr. Clifford then discussed pyramiding issues in New Mexico and highlighted some of the same points made by Mr. Anklam. The GRT accounts for more than 40 percent of all tax collections in New Mexico. The higher New Mexico sales tax offsets the lower-than-average property taxes the state imposes. The GRT tax base is composed of services (43 percent), retail (26 percent), construction (15 percent), wholesale (five percent), utilities (four percent), manufacturing (three percent) and other industries (four percent). The largest one percent of companies in New Mexico make up more than one-half of the GRT base, while the smallest two-thirds of companies make up less than one percent of the base. As a company size increases, the taxable share of its total sales decreases, because larger companies tend to export more.

Mr. Clifford gave an example of GRT pyramiding, describing all the business activities in producing electricity. Each time one business entity sells the product, it is taxed, which has the effect of raising the GRT rate on the final product from an average 7.4 percent to 13.88 percent. This effect can induce businesses to avoid the GRT by importing, or by bringing operations in-house. Although the overall business tax burden is about average nationally, the sales tax on business inputs is almost twice the national average. Businesses that purchase inputs from within New Mexico have a higher overhead than businesses that import. Depending on whether the seller has nexus in the state, this advantage can be either 2.5 percent or 7.5 percent.

Questions and comments from committee members included the following:

- Mr. Clifford was asked to provide a comparison of the amount of pyramiding in other states.

- Is pyramiding of the GRT passed on to consumers? Mr. Clifford said that this is difficult to determine, but said that increased GRT incidence reduces the total amount of sales.

- How could the state increase the percentage of property tax revenues going to the general fund? Mr. Clifford said that would require a constitutional amendment if the millage cap is increased. Mr. Anklam said that one idea raised in the past would be to impose a transfer tax on sales of real property. That idea met with stiff opposition from the real estate industry.

- If businesses pass on the pyramiding effects of doing business to consumers, how does that make a business less competitive? Mr. Anklam said that the pyramiding raises the final cost of the services or products being sold. The pyramiding effect depends on what is being produced and where the competitors are located.

- The claim that two-thirds of household spending is not taxed does not seem accurate. Mr. Clifford said that figure is the measure of direct GRT and does not include embedded GRT.

- Which sectors of the economy receive the biggest deductions from the GRT? Mr. Clifford said that the biggest deduction in the retail sector is on food. New Mexico does not have many deductions for services, which is the largest GRT sector. Most other states do not tax services. The committee member said that some business sectors cannot pass along the GRT.

- For every one percent increase in state taxation, the state gross domestic product decreases by .3 percent. Mr. Clifford said that studies of that type are very difficult to perform, but that figure seems plausible.

- The GRT deduction on food was supposed to pay for itself with the repeal of the .5 percent municipal credit. Mr. Anklam said that the state actually loses $150 million per year from that change in law.

- Do other states have different taxes that make up for the amount of money New Mexico raises from GRT pyramiding? Mr. Clifford said that is true, but now that internet transactions are increasing, the pyramiding effect in New Mexico is probably causing more economic distortions. Mr. Anklam said that New Mexico's tax burden is not transparent. Some industries win and others lose, based on the state's tax structure.

- If pyramiding is such a problem in the state, why are prices generally comparable with other states? Mr. Clifford said that for some businesses, pyramiding is a large burden. Most states do not tax services as much as New Mexico does, and every increase in the GRT rate compounds the pyramiding problem.

- The Taxation and Revenue Department (TRD) has a regulation that says winnings from a rodeo are subject to the GRT. A high school student who won purse money at a rodeo was recently fined by the TRD for not paying the GRT.

- If the state enacts laws that reduce the pyramiding effect on businesses, those businesses will end up paying more federal income tax, rather than paying the state taxes.

Tax Incentives

Dorothy Rodriguez, secretary-designate, TRD, presented a chart of 310 tax expenditures provided by New Mexico statutes. The chart was an expansion of the tax expenditure report discussed at the August meeting. Although tax expenditures account for a significant portion of a state budget, they often receive far less scrutiny than direct appropriations. There is no systematic review of tax expenditures, and there is no process to determine their effectiveness. She emphasized that the chart is still a work in progress, and there are many errors and gaps in data. The report is the TRD's draft of a tax expenditure report, which hopefully will be continued in the future.

The state has more information on credits because those amounts are often listed on tax returns. Deductions, however, are more difficult to track because they are often reported in the aggregate, and exemptions are usually not reported at all. Many of the exemptions and deductions are not really tax expenditures, but they are necessary to comply with federal law to reduce pyramiding and multiple taxation and to provide reciprocity with other states. As an example, the state provides an exemption from the GRT on wages because wages are already subject to other taxes.

Secretary-Designate Rodriguez described how other neighboring states track tax expenditures. Arizona provides a lengthy report of tax expenditures, but the report does not attempt to evaluate their effectiveness. Colorado produces a report of sales and use tax deductions and exemptions but also does not track effectiveness. Oklahoma provides a detailed listing of revenue foregone of about 450 tax statutes but does not evaluate their effectiveness.

Secretary-Designate Rodriguez presented a list of tax expenditure evaluation guidelines that New Mexico should consider adopting. She suggested developing a model statute for tax expenditures that would include the following elements:

- clearly defined purpose;

- application and claim procedures;

- clear definition as to how credits are calculated;

- certification requirements;

- carryforward rules (better to not allow carryforward);

- transferability (not preferred; this creates a secondary market for the credit at less than the full value of the credit);

- refundability (fully refundable credits are easier to administer but are essentially a cash subsidy);

- recapture or post-performance credit provisions;

- limits on use and duration;

- reporting requirements; and

- resources for administration and evaluation.

The model statute should also contain procedures for evaluating whether the objectives of the tax expenditures were accomplished. She suggested that credits not meeting the criteria specified have provisions for automatic repeal of those statutes. Reporting requirements need to be established in law, and sufficient resources and expertise need to be provided in order to allow the department to properly certify the credit applications.

Secretary-Designate Rodriguez said that the legislature should consider repealing Section 7-1-29.2 NMSA 1978, which automatically grants a credit if an application has not been reviewed by the TRD within 180 days. Finally, she suggested that a consensus group be established to continue the work of tax expenditure reporting, similar to the consensus revenue forecasting group already established.

Questions and comments from committee members included the following:

- Having a clearly defined purpose for tax incentives may conflict with the legislative tendency to not have purpose sections in statute.

- How should the reform recommendations be accomplished? Secretary-Designate Rodriguez said that a model statute should be drafted and existing credits should be conformed to the new standards. Enacting limits on some deductions and exemptions may also be appropriate to reduce the estimated $1.3 billion the state is spending.

- How is the TRD's tax amnesty program progressing? Secretary-Designate Rodriguez said that the department has received 2,000 claims so far in the program, and taxpayers have until September 30 to file claims.

- Are there any limitations on how many credits, exemptions or deductions a taxpayer can claim? Secretary-Designate Rodriguez said that, in general, if a taxpayer qualifies, there are no limits to how much a taxpayer can claim. She said that there are only a few credit exclusions in law.

- TRD staff was requested to consolidate some of the deduction and exemption categories in the report so it can be better understood.

- The RSTP should study the revenue impact on the state of rules proposed by agencies. Staff was instructed to investigate the possibility of legislation that would penalize state agencies that do not perform economic impact studies of proposed rules.

- Tax incentive law should include purpose sections in the legislation so that the incentives can be evaluated for effectiveness.

TRD Review — Summary and Discussion

Ms. Ray and Secretary-Designate Rodriguez discussed with the committee the structure and operational budget of the TRD. Ms. Ray began by stating that LFC staff has recommended that the premium tax, which is currently administered by the Public Regulation Commission, would be better administered by the TRD. The TRD consists of seven divisions and the Office of the Secretary. The five main functions of the TRD are tax administration, collection and disbursement; tax fraud elimination; motor vehicle control; property tax administration; and program support.

The department in fiscal year 2010 distributed $5.7 billion in tax revenue, more than 60 percent, or $3.7 billion, of which came from the GRT. Oil and gas revenues accounted for $860 million in distributions; the personal income tax (PIT) raised $336 million; combined fuel taxes raised $260 million; and motor vehicle fees and taxes raised $253 million. Other smaller tax programs include the weight distance tax, corporate income tax (CIT), gaming tax, cigarette tax, liquor excise tax and workers' compensation taxes.

The TRD has a total operating budget in fiscal year 2011 of $84.2 million, which is six percent smaller than the previous year. There are 1,183 total authorized full-time-equivalent (FTE) positions, which is 132 fewer than in fiscal year 2010. The TRD is implementing several budget reduction strategies, including:

- reducing the frequency of account statements from monthly to quarterly, although this may have a negative impact on audit and compliance collections;

- evaluating the need for driver's license and registration renewal notices to be mailed;

- closing one Albuquerque Motor Vehicle Division (MVD) office location;

- closing MVD field offices at 3:30 p.m. to eliminate staff overtime;

- discontinuing the printing of driver's manuals because they are available online;

- increasing the fee for the sale of data by $.50;

- implementing the Drive MVD program, which will include private operator driving test administration, more private retail agents across the state and fast-track services in 13 field offices for the disabled and elderly;

- reducing the number of PIT and CIT tax forms produced;

- reducing information technology maintenance agreements;

- restricting the use of supplies and inventory exempt purchases;
- using cash balances in the Property Tax Division for operating expenses;
- retaining a percentage of revenue from state-assessed property tax activities;
- keeping vacancies frozen in the Tax Fraud Investigations Division;
- increasing the use of electronic filing of returns by taxpayers;
- replacing the current customer call center with a more efficient system;
- redesigning the MVD web page, which will reduce customer demands on staff;
- redesigning the TRD intranet site to improve staff communications and reduce paper use; and
- redesigning the TRD web page for better customer service.

The TRD is also engaging in several revenue-enhancing efforts, including increasing delinquent collections and implementing the Fair Share Initiative, which has recurring costs of $5.1 million, has raised $21.3 million in fiscal year 2010 and is anticipated to raise $44.4 million in the current fiscal year. The department is also upgrading its compliance efforts by making upgrades to its data warehouse to better identify tax evaders; consolidating tax levy actions to increase efficiency; allowing tax collectors to have an overall view of a taxpayer's debts across tax programs; making upgrades to the bankruptcy program to ensure timely court filings; and increasing the use of payment plans for delinquent taxpayers.

Questions and comments from committee members included the following:

- Every new TRD employee generates significant revenue for the state. Revenue-generating state agencies should not have their FTEs cut because that will further reduce the state's revenues.
- How many new private MVD offices are being opened? Mike Sandoval, director, MVD, said that the MVD has just issued 10 to 12 requests for proposals (RFPs) for private MVD offices.
- TRD staff was asked to provide a cost-versus-revenue-raised report of an FTE employed by the MVD.
- Many state residents complain about poor services provided from state government, but few people are in favor of revenue-increasing measures. The PIT rates probably should be raised, but everybody is afraid of having that discussion. It costs much more to put somebody in prison than to provide that person a good education and decent health care.

- The only opportunity to reform state government is when there is a lack of money. Unfortunately, the state government merely seems to be rearranging itself, rather than engaging in true reform.

- The state needs to prioritize the most important functions of government, including education, health care and safe highways.

Committee members made recommendations for better tax administration, including:

- performing economic impact studies of proposed state agency rules;

- providing expiration dates and legislative review of tax credits;

- providing for a single state agency to track the effectiveness of all tax incentives; and

- using information technology improvements to save money, including the simple example of making direct deposits for legislative per diem reimbursements.

Department of Transportation (DOT) Review — Summary and Discussion

Ms. Ray and Secretary of Transportation Gary Giron discussed with the committee the structure and operations of the DOT and State Transportation Commission (STC). The STC is composed of six members appointed by the governor, one from each transportation district. Commissioners serve six-year staggered terms. The commission sets policy regarding the state's transportation system and oversees all expenditures from the State Road Fund (SRF).

The DOT is authorized by law to perform any of the duties assigned to the commission if the commission so designates those duties. The DOT consists of the Office of the Secretary, the Programs and Infrastructure Division and the Business Support Division. The DOT has its own treasury, which consists of the SRF, and it is allowed by law to have cash balances. This is due to the nature of financing for highway construction, which is typically on a reimbursement basis from the federal government. However, the department is required to have a balanced budget, so shortfalls in funding result in a reduction of road programs. In fiscal year 2009, the DOT had cash balances of $55 million, and cash balances totaled $102 million at the end of fiscal year 2010. The total state-funded budget for the department in fiscal year 2011 is $402 million. Federal funds for the year amount to $803 million.

The economic recession has impacted the DOT significantly. The department has cut 250 FTEs, all of which were vacant positions. This is a 23 percent reduction from the previous year's FTE authorization. Other reductions include:

- a 100 percent reduction in state-funded construction for roads that are not eligible for federal funding;

- a contract maintenance of highways reduction of $21 million in the past two fiscal years;

- heavy equipment replacement;

- winter services, including sweeping, guardrail repair, bridge deck preservation, striping, culvert cleaning and repair and provision of flashers and signals;

- spring activities, including chip seal application, pothole patching, equipment repair, mowing, sweeping, guardrail repair, dust storm mitigation, herbicide application and striping;

- summer activities, including chip seal application, road patching, blade patching, mowing, guardrail repair, dust storm mitigation and striping;

- overtime budgets, which resulted in reductions in snow removal and public safety and school safety programs; and

- operational and road maintenance budgets.

If revenue increases are not realized by the SRF soon, the DOT will be forced to make even more drastic cuts. There is no guarantee that federal highway funding legislation will be reauthorized, but even with that funding, the DOT faces huge shortfalls in highway repair, construction and maintenance funding. Secretary Giron said that there will be no new DOT construction programs in two years unless the federal or state government provides new revenue.

Secretary Giron discussed several revenue-raising options, including raising fuel taxes. New Mexico has the lowest gasoline tax in the region, and studies have shown that there is no direct correlation in the price of gasoline at the pump with the level of state taxation on gasoline. For every $.01 increase in the gasoline tax, the state would raise $8.3 million, and for every $.01 increase in special fuels taxes, $4.3 million would be raised. Secretary Giron noted that gasoline and special fuels taxes are assessed for every gallon of fuel sold. As vehicle efficiency standards have increased, less money is raised for each mile driven on the state highways.

Another option for raising money for the SRF would be to increase vehicle registration fees, which would raise $15 million for every $10.00 increase.

Questions and comments from committee members included the following:

- Has the DOT completed the purchase of the Lamy-Raton section of the Burlington Northern Railroad? Secretary Giron said that the purchase will be finalized next year, and $5 million has already been budgeted for that purchase. He said the state receives $2.5 million each year from the company for use of the Belen-Santa Fe portion of the tracks. The entire purchase price of the tracks was $75 million.

- Instead of cutting crucial services such as DOT funding, the legislature should focus on reducing waste in other sectors such as health care. Waste and fraud can be reduced without eliminating services.

- A small gasoline tax increase will not affect retail fuel prices but will significantly help the DOT annual budget shortfall.

- Has the department considered using toll roads to help its budget? Secretary Giron said that toll roads may be appropriate in a few areas of the state, but that will not address the overall statewide need for funding. The Federal Highway Administration has not authorized any new toll roads on interstate highways in a few decades. Mike Gibson of the Associated Contractors of New Mexico said that toll roads have consistently ranked lowest in polls for methods of raising revenue for state highways. He said that recent polling suggests that the public is in favor of increases in fuel taxes, if those increases are dedicated for highway maintenance and construction.

- Intermodal rail transport, which the state is prohibited from taxing, is reducing revenue to the state. DOT comptroller Greg Geisler said that he believes the interstate commerce clause of the federal constitution bars states from taxing rail transport. He said he will research that issue and confirm the answer for the committee.

- Some people claim that the reason Governor Bruce King lost his bid for reelection in 1994 was because he supported an increase in the gasoline tax, and any politician today supporting another increase is committing political suicide. However, there were many more important factors in Governor King's defeat, including the Indian gaming issue, the fact that the gasoline tax increase was distributed to the general fund and, probably most important, the presence of a strong Green Party candidate in the race.

- DOT staff was asked to provide a breakdown of each district's budget and any inter-district transfers. Staff was also asked to provide the number of lane miles in each district. Secretary Giron said that inter-district transfers are rare. He has been working with each district engineer to cut budgets.

- The idea that the government can spend money to create wealth is false. Spending money to prop up the economy has not worked.

- DOT staff was asked why there was a street sweeping crew in Encino during the legislator's commute to Santa Fe that day.

- DOT staff was asked to provide information on which road projects were deauthorized under the general language of "certain road projects" from the 2010 budgetary solvency package.

The committee recessed at 5:15 p.m.

Wednesday, September 15

The committee was reconvened by Representative Sandoval at 9:15 a.m.

Permanent Funds — Source, Earnings and Distributions

Commissioner of Public Lands Patrick H. Lyons and State Investment Officer Stephen K. Moise presented to the committee about state trust lands and income from permanent funds.

State Land Office (SLO)

Commissioner Lyons described the operations of the SLO and the history of the state's trust lands and how those lands are managed for trust beneficiaries. The U.S. Congress granted Sections 2, 16, 32 and 36 of every township in New Mexico for the benefit of public schools and other purposes, including universities; capitol buildings; charitable, penal and reform institutions; water reservoirs; Rio Grande improvements; and health institutions. The SLO manages lands owned by each beneficiary, and revenue raised on each property is credited to the beneficiary. The SLO manages 8.9 million acres of land in New Mexico, which is 11 percent of the total land in the state.

Revenue earned from state lands goes into two different funds, depending on the type of activity. Leases, rights of way, leasing bonuses and interest income are deposited into the Land Maintenance Fund (LMF). The SLO reserves two percent of the revenue for its operations, and the rest is distributed to the beneficiaries. The public school distributions are deposited into the general fund. Royalties from mineral and oil and gas extraction activities and land sale proceeds are deposited into the Land Grant Permanent Fund (LGPF), which is managed by the State Investment Office (SIO). Distributions are made to trust beneficiaries of a percentage of income earned from the fund, according to the amount invested on behalf of each beneficiary. Distributions for the public schools are made into the Common School Fund. The vast majority of distributions goes to the Common School Fund.

Annual distributions from the LMF have varied between $28 million to fiscal year 2010's distributions of $76 million. Total distributions in the last eight fiscal years were $417 million. Distributions from the LGPF have steadily increased from $333 million in fiscal year 2003 to $526 million in fiscal year 2010, although a large portion of the increase was attributable to the adopted constitutional amendment that increased the percentage of the distribution to public schools for several years.

Oil, gas and mineral extraction activities account for 95 percent of the income earned by the SLO. Other sources of income include renewable energy, rights of way, community and business development and agricultural leases. Total revenue earned by the SLO has increased from $263 million in fiscal year 2003 to a peak of $546 million in fiscal year 2008. Fiscal year 2010 revenues were $420 million. The operating budget for the SLO has remained flat for the past fiscal year at $13.9 million. The office has reduced the number of FTE positions, and no employee earns more than $100,000 per year.

State Investment Council (SIC) Overview

Mr. Moise described the functions and structure of the SIC, which was recently reorganized by the legislature. The council is composed of 11 members, including the governor, the secretary of finance and administration, the state treasurer, the commissioner of public lands, a university representative, two public members appointed by the governor and four public members appointed by the New Mexico Legislative Council. Public members must be confirmed by the senate, have extensive investment or finance experience and have no previous contracts with state investment, and they are precluded from having investment contracts with the state two years following their service. The SIC has investment oversight and approval powers and has the power to appoint the state investment officer. The officer oversees the day-to-day operations of the SIO. Currently, the SIO has 30 full-time employees.

The SIO manages approximately $13.7 billion in assets, including the LGPF, the Severance Tax Permanent Fund (STPF), the Tobacco Settlement Permanent Fund, the Water Trust Permanent Fund and investment assets of 19 other state and local government clients. Fifty-six percent of the SIO's investments are in public equities; 18.5 percent are held in bonds; and 23.5 percent are invested in alternatives, including private equities, hedge funds and real estate. The office also has the ability to invest a certain percentage of the STPF in economically targeted investments, including nine percent of the fund in New Mexico private equity funds; six percent in film loan investments; and 20 percent in New Mexico bank certificates of deposit (CDs). Mr. Moise said that the state has not yet earned any money from film investments. The bank CD program has just begun, and the SIO has not yet invested any money in the program. The state has invested $289.9 million in New Mexico private equity funds.

Distributions from the state's two largest permanent funds, the LGPF and the STPF, have totaled $3.4 billion in the past five years. The current distribution rate from the LGPF is 5.8 percent of the five-year fund average. That rate will decline to 5.5 percent in fiscal years 2013 through 2016 and further decline to 5.0 percent beginning in fiscal year 2017. The STPF distribution rate is set at 4.7 percent of the five-year fund average and has totaled $909 million in the past five years. Money from the fund is distributed to the general fund. Mr. Moise cautioned that the current level of distributions from the fund will be difficult to maintain in the upcoming years.

The previous state investment officer had set a long-term annual investment return goal for the SIO's assets of 8.5 percent. Mr. Moise said that rate is no longer realistic. The SIC will soon set a new investment goal, probably at 6.5 percent or seven percent. That new estimate will have significant effects on future distributions from the funds and will be aggravated by scheduled reductions in the percentage of distributions from the LGPF.

Mr. Moise said that the SIO just hired a film investment auditor to ensure that the office receives adequate returns from its film investments. The office also recently hired Vince Smith, former state investment officer of Kansas, to be the deputy state investment officer.

Questions and comments from committee members included the following:

- Is the state getting its money's worth from film investments? Mr. Moise said that the audit process is just being established and that the state should be seeing some revenue soon from the process.

- How did state trust lands get designated? Commissioner Lyons said that each beneficiary chose its lands in 1913. Any money earned from a piece of land is designated for that particular beneficiary, either as a monthly check from the LMF or as a percentage of its investment in the LGPF.

- Is income from renewable energy increasing? Commissioner Lyons said that the SLO has four wind farms on its land. The problem with getting more wind farms is the difficulty in obtaining financing and the lack of transmission lines to suitable locations.

- Would the SIC be interested in investing in New Mexico wind farms on state trust lands? Mr. Moise said that he would investigate that possibility.

- Which entity receives distributions for the New Mexico Boys' School at Springer since that school is no longer open? Commissioner Lyons said that the money has been designated toward a school in Albuquerque operated by the Children, Youth and Families Department.

- Has there been much new interest in oil and gas leases? John Bemis of the SLO said that there has been much renewed interest in extraction leases. The SLO earned $62 million in oil and gas bonuses last year, which was a new record. Bonus income is deposited into the LMF.

- How are the state charitable institutions determined? Commissioner Lyons said that seven entities were named in the Enabling Act for New Mexico. In order for any new entities to be named, the voters would have to approve a constitutional amendment and the U.S. Congress would have to approve an amendment to the Enabling Act.

- Was the previous 4.7 percent distribution rate from the LGPF based on an expected 8.5 percent annual rate of return from investing the fund? Charles Wollman from the SIO said that he believes that the 8.5 percent target was set by the previous state investment officer. However, prior to 2003, the Public Employees Retirement Association (PERA) and the Educational Retirement Board (ERB) each had investment targets of eight percent.

- Does the SIO charge a fee for managing the assets of other entities? Mr. Moise said that the SIO is reimbursed for direct costs associated with managing the funds, depending on the investment class. Most entities pay less than 25 basis points (.25 percent) of the investment.

- SIO staff was asked to provide a complete list of its government clients.

- The SIO needs to invest money in New Mexico bank CDs to encourage lending to local businesses. Mr. Moise said that there has to be a balance between maximizing investment returns with other policy goals.

- Can the state borrow money against the balance of the LGPF or the STPF? Mr. Moise said that he is not aware of that possibility.

- Although the average 19 basis points that the SIO pays to its investment managers seems low, that rate amounts to more than $26 million. The SIO should do a better job of negotiating investment fees because it has such a large portfolio. Mr. Moise said that the SIO is constantly negotiating fees with its managers.

- What percentage of the SIO's real estate investment portfolio is in real estate investment trusts (REITs)? Mr. Moise said that he does not think the SIO has any REIT investments, but he will verify that information and report back to the committee.

- What has been the rate of return in the SIO's investment in private equities? Mr. Wollman said that the office has seen an average nine percent investment return. New Mexico private equities have not yet earned a profit, mostly because they have not been sold off.

- Can the functions of the SIO be combined with the PERA and the ERB? Mr. Moise said that there are many synergies with those entities, and some functions could be shared. He said that he is not sure whether any benefit would be gained from combining the entities, but the the RFP process and legal services could be combined easily.

- Should the responsibility for making economically targeted investments be moved to the Economic Development Department, as those investments may be at odds with the overriding goal of earning as much money as possible for the beneficiaries? Mr. Moise said that those investments require much time to manage, but he had no recommendation about which entity should manage them.

PIT and CIT Proposals — Council on State Taxation Ranking

James P. O'Neill, consultant, presented two legislative proposals designed to easily improve New Mexico's ranking as a good place to do business. The Council on State Taxation publishes a report that ranks states according to how difficult a state taxation department is to deal with from a business point of view. The council has several criteria to measure how business-friendly a state is for tax appeals and general administrative practices, including whether the state has an independent tax dispute forum, whether a business is required to post bond to file an appeal, whether there is even-handed treatment of refunds and assessments, the number of days allowed to protest an assessment and how long a taxpayer has to file with the state after a final determination of federal tax changes has been made.

Mr. O'Neill presented two bill drafts that attempt to mitigate several of the findings of the council. The bills:

- extend the deadline for reporting federal tax status changes from 90 days to 180 days, clarify what changes need to be reported and define "final determination" according to the council's preferred standard;

- extend the grace period from 30 days to 90 days before a taxpayer becomes delinquent;

- extend the time for protesting from 30 days to 90 days;

- extend the time allowed to claim a refund to three years to match the TRD's time frame to make an assessment; and

- extend the reporting date for CIT reporting by an extra month.

There being no further business, the committee adjourned at 11:50 a.m.

REVENUE STABILIZATION AND
TAX POLICY COMMITTEE

Section 7

October 2010
Agenda
Minutes

Revised: October 21, 2010

TENTATIVE AGENDA
for the
FIFTH MEETING IN 2010
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

October 25-26, 2010
Room 322, State Capitol

<u>Monday, October 25</u>

9:00 a.m. **Call to Order**
—Representative Edward C. Sandoval, Chair

9:05 a.m. **Tobacco Settlement Permanent Fund Receipts — Definition Change**
—Al Lama, Chief Deputy, Office of the Attorney General

9:30 a.m. **Revenue Forecast and Fiscal Update**
—Dorothy Rodriguez, Secretary-Designate, Taxation and Revenue Department (TRD)
—Dannette K. Burch, Secretary-Designate, Department of Finance and Administration
—Tom Clifford, Chief Economist, Legislative Finance Committee (LFC)

10:45 a.m. **Laboratory Partnership with Small Business Tax Credit — Annual Report**
—Genaro Montoya, Program Leader, New Mexico Small Business Advocates, Sandia National Laboratories
—Mariann Johnston, Los Alamos National Laboratory

11:30 a.m. **Business Incentives Most Commonly Used for Economic Development**
—Larry Horan, Lobbyist, Eastern New Mexico Economic Development Association
—Brandon Honea, KPMG
—Pat Vanderpool, Tucumcari Economic Development
—Debra Inman, Albuquerque Economic Development
—Ned Godshall, President and CEO, Altela
—Brenda Miller, Director of Human Resources, Southwest Cheese
—Tim Van Valen, Attorney, Brownstein Hyatt Farber Shreck

12:30 p.m. **Lunch**

1:45 p.m. **Property Tax Legislation — Fiscal Impact Report Review**

—Tom Clifford, Chief Economist, LFC
—Julie Anna Golebiewski, Senior Economist, LFC

3:00 p.m. **Property Tax — Issues and Proposals**
—James P. O'Neill, Consultant
—Al Maury, Senior Policy Analyst, TRD
—Ron Lethgo, Chaves County Assessor, Chair, New Mexico Association of Counties President's Property Tax Committee

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

Tuesday, October 26

9:00 a.m. **Reconvene**
—Representative Edward C. Sandoval, Chair

9:05 a.m. **Manufacturing, Distribution and Logistics on the Border — Personal Income Tax and Corporate Income Tax Credits**
—Juan Massey, Director, Regulatory Affairs, Verde Realty
—Jerry Pacheco, Vice President, Border Industrial Association

10:05 a.m. **Use of Alternative Energy Tax Credits**
—Annie Carmichael, Lobbyist, Sun Edison

11:05 a.m. **Jet Fuel Gross Receipts Tax Credit Sunset**
—Ed Mahr, Lobbyist, Southwest Arilines

12:05 p.m. **Lunch**

1:20 p.m. **Federal Low Income Housing Credit Use in Valuation of Property**
—Steve Natelson, Attorney

2:20 p.m. **Above-Ground Storage Tanks**
—Senator John M. Sapien
—Cyndee Biggers, Petroleum Distribution Manager, Bowlin Travel Centers
—Scott Scanland, Lobbyist, Bowlin Travel Centers

3:20 p.m. **Adjourn**

MINUTES
of the
FIFTH MEETING IN 2010
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

October 25-26, 2010
Room 322, State Capitol
Santa Fe

The fifth meeting of the Revenue Stabilization and Tax Policy Committee (RSTP) for 2010 was called to order by Representative Edward C. Sandoval, chair, on Monday, October 25, 2010, at 9:20 a.m. in Room 322 of the State Capitol in Santa Fe.

Present
Rep. Edward C. Sandoval, Chair
Sen. John Arthur Smith, Vice Chair
Sen. Carlos R. Cisneros
Rep. Nathan P. Cote (10/26)
Rep. Anna M. Crook
Sen. Tim Eichenberg
Rep. Keith J. Gardner
Sen. Timothy Z. Jennings
Sen. Timothy M. Keller
Sen. Gay G. Kernan (10/25)
Rep. Ben Lujan, Speaker of the House
Rep. Rodolpho "Rudy" S. Martinez
Sen. Howie C. Morales
Rep. Henry Kiki Saavedra
Rep. Thomas C. Taylor
Rep. Jim R. Trujillo

Absent
Sen. Dianna J. Duran
Sen. William E. Sharer

Designees
Sen. Mark Boitano
Sen. Kent L. Cravens (10/26)
Sen. Phil A. Griego (attending as a guest)
Sen. Clinton D. Harden, Jr.
Rep. Debbie A. Rodella (attending as a designee 10/25 and as a guest 10/26)
Sen. Nancy Rodriguez (attending as a guest)

Rep. Ray Begaye
Rep. Donald E. Bratton
Rep. Zachary J. Cook
Rep. Miguel P. Garcia
Rep. Roberto "Bobby" J. Gonzales
Rep. Sandra D. Jeff
Sen. Carroll H. Leavell
Rep. Antonio "Moe" Maestas
Sen. Steven P. Neville
Sen. Bernadette M. Sanchez
Sen. John M. Sapien
Rep. James R.J. Strickler
Rep. Don L. Tripp

Rep. Luciano "Lucky" Varela
Sen. Peter Wirth

Other Legislators Attending
Rep. Ernest H. Chavez (10/26)
Sen. Cisco McSorley (10/25)

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

Staff
Pam Ray, Legislative Council Service (LCS)
Doris Faust, LCS
Ric Gaudet, LCS

<u>Monday, October 25</u>

Tobacco Settlement Permanent Fund Receipts — Definition Change

Betsy Glenn, deputy attorney general, and Nan Erdman, assistant attorney general, presented a proposed definition change in cigarette tax statutes. Ms. Erdman said that a mistake was made during the last legislative session when cigarette taxes were raised. The result of that legislation is that some cigarette companies are no longer required to deposit a percentage of their cigarette sales on tribal lands into an escrow account. In 1999, New Mexico entered into the Master Settlement Agreement (MSA) with major tobacco companies that required companies to pay the state for every cigarette sold. Since then, more than 50 companies have joined the settlement. One of the conditions of the settlement was that New Mexico enact a statute requiring that nonparticipating companies contribute to an escrow account a percentage of their cigarette sales. This was needed in order to remove the competitive advantage that nonparticipating companies would otherwise have.

In 2010, the legislature raised the cigarette tax but provided for the same 91-cent differential between tribal and nontribal sales. By adding an additional category of cigarette tax stamp and stating that it was not an excise tax stamp pursuant to the Cigarette Tax Act in Chapter 7 NMSA 1978, confusion occurred over the definition of "units sold", a term used in the nonparticipating manufacturers' escrow statutes in Chapter 6 NMSA 1978. The question was whether the cigarettes sold by nonparticipating manufacturers were still considered to be stamped with "tax exempt" stamps. Tax-exempt stamped cigarettes are explicitly mentioned in the definitions of "units sold", thus allowing any cigarettes sold in a pack bearing a tax-exempt stamp to be counted toward the number of units sold in the state for purposes of determining escrow payments. The question has allowed nonparticipating manufacturers to argue that because some of their cigarettes are sold with tax-credit stamps, they are not tax-exempt stamps under the definition of "units sold" and are therefore not counted for purposes of payment of escrow. The Office of the Attorney General (AGO) wants to be certain that the escrow requirement is in statute. The office also wants to require that tobacco products sold by tribes be on the approved list of tobacco products, which will ensure that dangerous chemicals are not added to tobacco products sold in the state.

Ms. Erdman said that participating companies are alleging that New Mexico is not diligently enforcing the settlement. Nonparticipating companies are using tribal lands to import cigarettes without collecting the escrow amount. If the participating companies prevail in their case, New Mexico stands to lose annual tobacco settlement funds paid to be the state as well as escrow payments beginning July 1, 2010.

Questions and comments from committee members included the following:

• A committee member said that he had asked a representative of the AGO during the legislative session whether the cigarette-tax-raising proposal would have any effect on the MSA. The AGO representative had indicated that there were no problems with the legislation. Ms. Erdman said that the person who had testified before the legislature no longer works with the AGO. She said that she had not seen the legislation before it was voted on by the senate. The 2010 change in statute effectively undid the change made in 2009, which required that tribal sales by nonparticipating companies have the escrow requirement.

• How is the escrow amount collected? Ms. Erdman said that escrow money is not a payment to the state, but the money is set aside if the state decides to sue nonparticipating companies for the costs the state incurs as a result of cigarettes being sold. The cigarette taxes are paid to the state or tribes by the distributor of the cigarettes. MSA payments are made by cigarette manufacturers to the state. The average MSA contribution is about $5.30 per carton sold in the state.

• The AGO had plenty of time during and after the session to ensure that the language in the cigarette tax bill was adequate. For example, the bill was in the House Taxation and Revenue Committee for three days. The AGO staff should have done a better job.

• How are the tax-credit stamps created by the new legislation regulated, and how are illegal cigarette shipments stopped? Ms. Erdman said that a distributor receives a tax-credit stamp for tribal sales if the tribe imposes a tribal cigarette tax. Illegal shipment of cigarettes has been a big problem in the past. The AGO has managed to shut down some companies that were importing cigarettes illegally. The new legislation proposed by the AGO will address the illegal cigarette problem somewhat, and it will actually reduce the work load of the office.

• How much money is currently in the escrow account? Ms. Erdman said that there is approximately $72.8 million in the account. Interest in the account is returned to the manufacturers.

• Why has the state not sued the nonparticipating manufacturers? Ms. Erdman said that the AGO does not have enough resources to pursue that litigation.

Joe Thompson, a lobbyist representing Native Traders, a nonparticipating tobacco company, said that his company has a much different perspective on the AGO's legislation.

He said that the escrow requirement change was not an oversight at all; rather, it was part of the deal that made the legislation acceptable to the parties. He said that the change proposed by the AGO would be a betrayal of the deal made with the tribes.

Revenue Forecast and Fiscal Update

Dorothy Rodriguez, secretary-designate of taxation and revenue, Dannette K. Burch, secretary-designate of finance and administration, and Tom Clifford, chief economist, Legislative Finance Committee (LFC), presented a revenue forecast and fiscal update to the committee. The forecast was developed by the Consensus Revenue Estimating Group, consisting of career economists at the Department of Finance and Administration (DFA), the Taxation and Revenue Department (TRD), the Department of Transportation (DOT) and the LFC. Secretaries-Designate Burch and Rodriguez presented the revenue estimate first.

Changes in the revenue estimate from July 2010 indicate that fiscal year 2011 revenues will decrease another $40 million and that projected revenues for fiscal year 2012 will decrease $81 million. Weaknesses in gross receipts and selective sales taxes were important factors in the downward revision of the fiscal year 2011 estimate. General fund reserves are expected to drop an additional $18.5 million from the July estimates, which leaves a 3.5 percent reserve level at the end of fiscal year 2011. The administration was granted authority to adjust budgetary allotments downward, but the administration does not currently propose such a move because agencies have already been preparing for a mid-fiscal-year reduction in their budgets of three to five percent.

The key economic indicators for New Mexico predict that the decelerating growth observed in the second and third quarters of 2010 will not likely result in a "double-dip" recession. Although the state's gross domestic product (GDP) grew by less than one percent in fiscal year 2010 and employment is not expected to grow at all in fiscal year 2011, personal income is expected to grow in fiscal years 2011 and 2012, averaging between two and three percent. Nonagricultural employment in fiscal year 2010 fell 3.3 percent. Inflation is expected to remain below two percent in fiscal years 2011 and 2012.

General fund revenue estimates have not changed substantially from the July 2010 estimate. The estimate for fiscal year 2011 totals $5.11 billion, which is three percent less than fiscal year 2010. Recurring revenues to the fund are projected to grow by six percent from fiscal year 2010 levels; however, federal stimulus funding from fiscal year 2010 is no longer available for the current fiscal year. Total revenues to the general fund in fiscal year 2012 are expected to be $5.36 billion, a five percent increase from the current fiscal year. Annual growth to general fund revenues are expected to be at four percent during fiscal years 2013 through 2015.

Mr. Clifford then presented the LFC's analysis of the revenue estimate. The key points of the analysis include:

- Fiscal year 2010 revenue was $172 million less than appropriations.

• Fiscal year 2011 revenue, after authorized reserve transfers and allotment reductions of $151 million, is $17 million less than appropriations.

• Fiscal year 2012 revenues are predicted to be $258 million below the cost of current services. Those revenues include the replacement of $350 million in federal Medicaid and public school funds.

• While general fund recurring revenue fell by more than 20 percent from fiscal years 2008 to 2010, total spending, including federal temporary funding, actually increased during those years.

• Gross receipts tax (GRT) revenue declined by more than 10 percent in fiscal year 2010. GRT revenue is expected to increase by three percent in fiscal year 2011 and by four percent in fiscal year 2012.

Questions and comments from committee members included the following:

• The projection of personal income tax (PIT) growth over the next few fiscal years seems overly optimistic. Sam Flame, chief economist, DFA, said that the indicators predict that New Mexico should be seeing increases in employment, which correspond to PIT levels.

• New Mexico tends to enter and exit from recessions later than the rest of the nation. Mr. Clifford agreed, and he said that he prefers to use employment trends in addition to GDP levels. He said that increases in oil and gas production do not necessarily mean that more jobs are created. New Mexico has not yet reached positive growth in employment, but the rest of the country did so several months ago.

• Many of the cuts to public education in the past two years have been more than offset by federal Title 1 and stimulus funding, which is distributed directly to school districts. Some districts have realized unprecedented levels of funding. DFA and LFC staff were asked to provide a listing of total funding for public schools, not just general fund appropriations.

• Did the consensus revenue economists assume zero percent economic growth in the next fiscal year? Mr. Clifford said that the fiscal year 2012 scenario is essentially a no-growth estimate.

• Why did the corporate income tax (CIT) revenues show such a strong growth? Mr. Clifford likened the CIT growth, from almost nothing to a small amount, to the observation that "even a dead cat will bounce".

• If the legislature replaces temporary federal funding, that will make the services provided permanent.

Laboratory Partnership with Small Business Tax Credit — Annual Report

Genaro Montoya, program leader, New Mexico Small Business Advocates (NMSBA), Sandia National Laboratories, and Mariann Johnston, Los Alamos National Laboratory (LANL), presented the annual report of the laboratory partnership with small business tax credit program to the committee. Mr. Montoya stated that the NMSBA is a catalyst for the transfer of cutting-edge technology from the state's national laboratories to a wide range of small businesses across the state. The tax credit allows each national laboratory to claim up to $2.4 million per year in expenses for assisting small businesses. Rural businesses are allowed up to $20,000 per year in assistance, and small businesses in urban counties can receive $10,000 in assistance.

Between 2000 and 2009, $20.6 million in assistance was provided to 1,597 small businesses in 32 of the state's 33 counties. So far in 2010, $4.2 million in assistance has been provided to 301 small businesses. The NMSBA studies the economic impact of the tax credit. It estimates that 1,549 jobs in 2010 were created or retained as a result of the business assistance. The return on investment realized by the state from the credit is estimated to be $1.24 for every dollar of credit.

Ms. Johnston described different industries that are benefiting from the assistance provided by the laboratories. The NMSBA is helping companies develop technologies to treat and reuse produced water from oil and gas operations. Businesses in the Roswell area are also getting help in developing technology to more precisely locate bypassed petroleum deposits in the Permian Basin. The NMSBA is helping the renewable energy industry by assisting with biofuel production, solar thermal and wind turbine design improvements and evaluation of landowner potential for wind and solar energy generation, production and distribution. The NMSBA is also helping the agricultural industry: providing assistance on projects to manage surface water quality, reservoir storage and water delivery schedules; developing a new bovine tuberculosis test; treating ground water for high sulfates to protect cattle health and reproduction; and developing tools to differentiate between dairy and nondairy contributions to nitrate contamination in ground water.

Ms. Johnston introduced Jay Lazarus, owner of Glorieta Geoscience, a ground water consulting company. The company has received technical assistance from LANL to perform forensic research on dairy isotopes to specifically identify nitrate contamination sources. Many feedlot dairies are under ground water contamination abatement orders by the Department of Environment (NMED), and if the nitrate contamination from previous chemical fertilizer use can be differentiated from the current nitrate contamination from the dairies, the industry could get relief from the strict requirements. LANL is helping Glorieta Geoscience develop its technical capabilities to identify those nitrates, he said.

Committee members lauded the laboratories for their exemplary work in assisting small businesses in New Mexico.

Business Incentives Most Commonly Used for Economic Development

The committee heard from a panel of business owners and leaders about important business incentives. Larry Horan, lobbyist, Eastern New Mexico Economic Development

Association, introduced the members of the panel and said that the panel's intention was to educate the committee about the most important statutory business incentives and how they are being used.

Pat Vanderpool of Tucumcari Economic Development said that the goal of economic development organizations is to increase employment and income in communities through business recruitment and retention efforts. The most important business incentive is the job training incentive program (JTIP), which provides training funds for new employees. Other important incentives include the high-wage jobs tax credit and the investment credit. The economic development community needs to use every tool available to attract and retain businesses, he said.

Debra Inman of Albuquerque Economic Development discussed three potential business relocations that Albuquerque recently lost. Soladyne Capital, an insulated-glass manufacturer, recently decided to locate a facility in Mississippi instead of New Mexico, partially because better incentives were offered by that state. The state also lost an opportunity to Michigan when Suniva, a photovoltaic manufacturing company, decided to locate there. A third company, whose name has not yet been disclosed, recently decided not to locate in New Mexico, costing the state 500 jobs.

Doug Penner of Altela, a company specializing in water desalinization and produced water purification, discussed the incentives of which his company has taken advantage. Altela started operations in 2005 and has 25 employees. Prior to the recent economic downturn, the company had 50 employees. Currently, the company is in a gradual hiring phase. Altela uses JTIP funding, the high-wage jobs tax credit, the investment credit and the technology jobs tax credit.

Brenda Miller, director of human resources, Southwest Cheese, told the committee that her company located in New Mexico instead of Texas because of the incentives New Mexico provided as well as the long-term advantages the state offered. Southwest Cheese has 324 employees and processes 11 million pounds of milk per day. New Mexico now ranks seventh in the nation in milk production, and the state has surpassed Wisconsin in cheese production. The company uses JTIP funding, the high-wage jobs tax credit and industrial revenue bonds.

Brandon Honea of the global tax, audit and advisory firm KPMG said that he performs site selection services for clients seeking to locate their businesses. The firm performs comparative analyses and modeling of the business climate in different states, including the level of tax incentives available. KPMG was responsible for bringing the Hewlett-Packard call center to New Mexico, creating 1,800 jobs. He said that tax credits make a good site better, but they do not make a poor site into a good one. Nationally, two kinds of incentives work well in attracting businesses: cash grants and payroll tax credits. New Mexico has a very competitive set of incentives, and he recommended that those incentives be continued.

A committee member commented that the legislature does not appreciate it when companies come to New Mexico for a few years and then leave for better pastures in other states. Call centers have earned a poor reputation in rural areas. The committee member also said that industrial revenue bonds have the effect of raising property taxes on everybody else.

Property Tax Legislation — Fiscal Impact Report Review

Mr. Clifford and Julie Anna Golebiewski, senior economist, LFC, presented to the committee a review of property tax "lightning" legislation introduced in the last regular session of the legislature. Property tax lightning refers to large differences in the property tax valuation of two otherwise similar properties. Section 7-36-21.2 NMSA 1978 limits the annual growth in valuation of certain properties to three percent per year. Other properties, especially properties that change owners, are assessed at the full market value. If the market value of properties grows more than an average of three percent, the disparity between valuations grows over time. Ms. Golebiewski began with an overview of the legislation. Both retroactive and prospective remedies were proposed, with a wide variety of fiscal impacts. With all of the legislation, some taxpayers would see tax increases and some would see decreases. The constitutional status of the current law, as well as the new proposals, remains uncertain.

A survey of other states' laws regarding property tax lightning showed that 20 states have some kind of valuation limitations. Most of those states restrict the annual growth rate to between two percent and 15 percent. Some states do not require the correct valuation of properties upon sale.

Mr. Clifford discussed some of the issues addressed by the seven property tax lightning bills in the previous legislative session. All of the bills proposed equal treatment of property valuations prospectively, at least for existing properties. Prospective remedies do not address the existing gap from differential valuations from 2004 to the present.

Two bills proposed retroactive remedies by bringing all assessed values to today's market values, then applying growth limits in the future. The LFC estimated that this would cause a 14 percent increase in statewide residential taxable value in the first year. Properties that currently enjoy limitations in valuations would see a five to 10 percent increase in tax payments, while those properties currently valued at market values would see a 10 to 15 percent decrease in property tax payments. In addition, the statewide general obligation bond capacity would increase by approximately $40 million.

Two bills proposed retroactive remedies by lowering the assessed values of properties sold after 2004 to a rate not exceeding three percent per year. The LFC estimated that this method would result in an average six percent increase for currently limited property owners.

Another bill proposed limiting valuations only to the constitutionally mandated categories of age, income and owner occupancy, rather than having statutory limitations that provide no distinction between owner-occupied and rental properties. In order to implement this provision, county assessors would need to obtain accurate data on the residency status of properties.

One bill attempted to address valuation disparities that happen between new construction and existing properties by adjusting new construction assessments toward existing properties' assessed valuations. The problem with this approach is determining how to find comparable properties for valuation purposes.

Overall, the fiscal impact of most of the bills would be that the current beneficiaries of valuation limitation would see increases in their property taxes, but government revenue would be generally the same. However, some governmental entities that are currently at their maximum rate level could see revenue decreases, but those impacts would be small. All bills would reverse the inequity that exists in current law.

Questions and comments from committee members included the following:

- How do New Mexico's property taxes rank in comparison to other states? Mr. Clifford said that the state ranks pretty low nationally, but Bernalillo County property taxes are about twice that of the rest of the state.

- There is a policy disagreement about whether new construction should be valued at its market value when it enters the tax rolls, or whether comparable values should be used.

- How will the new real estate transaction fees for Medicare, recently enacted by Congress, affect homeowners in New Mexico? Mary Martineck of the New Mexico Realtors Association said that she would provide the committee with information on that new tax. She said that most real estate transactions would not be covered by the new law. (The following day, she presented a fact sheet that stated that real estate sales that result in a net capital gain above $250,000 for individuals who have an adjusted gross income above $200,000 would be subject to a 3.8 percent tax on those capital gains above $250,000, beginning in 2013.)

Property Tax — Issues and Proposals

The committee heard a presentation and discussion of solutions to the property tax lightning problem. James P. O'Neill, consultant, began the presentation by reminding the committee that Article 8, Section 1 of the Constitution of New Mexico requires the legislature to enact property tax valuation control. Any solution enacted to fix the current problem with Section 7-36-21.2 NMSA 1978, portions of which were determined by two district judges to be unconstitutional, will necessarily make a portion of residential homeowners pay higher property taxes. He cautioned against a solution that would reduce or hold harmless property taxes for all residential properties because county governments rely almost completely on property tax revenues for their budgets.

Gary Perez, Dona Ana County assessor, discussed two legislative solutions developed by the New Mexico Association of Counties (NMAC) President's Property Tax Committee. He said that the goal of assessing similar properties similarly directly conflicts with the goal of insulating long-term homeowners from the tax effects of market increases. There are several sections of law that need to be considered in order to understand the situation. Section 7-36-16 NMSA 1978 requires county assessors to maintain current and correct valuations of property. However, Section 7-36-21.2 NMSA 1978 limits to no more than three percent the annual valuation increases of certain classes of residential property. Section 7-36-21.3 NMSA 1978 provides for no property valuation increases for low-income elderly or disabled homeowners. Section 7-37-7.1 NMSA 1978 limits the increase of property tax revenue to no more than the percentage increase from new construction plus inflation. This provision is commonly referred to as "yield control".

The first option, which is the most favored choice of county assessors, would be to amend Article 8, Section 1 of the Constitution of New Mexico to eliminate the mandatory limits on valuation. If the amendment is adopted by the voters in 2012, then the legislature would eliminate or increase the annual valuation cap; require county assessors to bring all property valuations to their market value; and set the yield control inflation factor to zero for the first year, which would have the effect of maximizing the rate-reduction effect. This method would establish a permanent process for equalizing valuations and would not discriminate against new construction. However, property taxes would rise significantly for those properties that are undervalued.

The second option would consist of statutory changes only and is the choice of the NMAC committee. County assessors would bring all property valuations to current and correct levels; the yield control inflation factor would be set to zero; and the valuation cap would be converted from a full value cap to a taxable value cap, perhaps set at a different percentage increase level. The last provision would allow the full valuation of properties to be displayed, along with the taxable value of those properties, and would allow county assessors to maximize the use of computer-aided mass appraisal (CAMA) systems. This solution has the same drawback as the first solution: long-term residential homeowners would see significant increases in valuation and tax assessments.

Questions and comments from committee members included the following:

- Committee members expressed their desire to meet with the key stakeholders in this issue.

- Some counties do not have CAMA systems. Would this become a barrier to the implementation of either solution? Mr. Perez said that either option can occur with current technology. He said that the NMAC committee is looking for direction from the RSTP about which option to pursue in the upcoming legislative session.

- When the current three percent valuation limitation was enacted, county assessors were supposed to bring all property valuations to current and correct levels before imposing the limitation, but that did not happen. What assurances are there that they would bring properties to the correct level if new statutory changes are made? Mr. O'Neill said that the requirements of valuations would need to be specified in the legislation.

- Glenn Walters, county commissioner, Sandoval County, said that fixing the property tax lightning issue is the top legislative priority of the NMAC. He acknowledged that adopting a constitutional amendment would be difficult.

- Any solution to the property tax lightning problem needs to address the decade-long overpayment of property taxes by some homeowners.

- Both options would need a phase-in period to make them palatable to homeowners.

- Any solution to the property tax lightning problem needs to ensure that there will be no
net increase in tax revenue to local governments during the transition period.

- Staff was directed to ask for an attorney general's opinion on whether the legislature can roll back property tax valuations to previous levels. Mr. Perez said that there is also a language disparity between the constitution and statutes between "owner-occupied" and "residential" that should be remedied.

Mr. O'Neill then presented a proposal to clarify the calculation of mill rates pursuant to the yield control law (Section 7-37-7.1 NMSA 1978). The primary change in the law would be to differentiate the calculation of "net new value" and "valuation maintenance". This change would allow counties to set mill rates much easier than with the current system.

Al Maury, senior policy analyst, TRD, briefly presented an update to the committee of recent property tax data. Net taxable value of all property in New Mexico's tax system in 2010 is approximately $50.5 billion. This value is 7.2 percent less than the total taxable value in 2009. The drop in values is almost entirely due to the large decline in oil and gas production, which determines the amount of ad valorem and equipment property tax paid. Residential and commercial valuations increased an average 1.3 percent from 2009. In 2010, tax obligations are estimated to be $1.5 billion, which is four percent less than in 2009. The average mill rate for all properties in 2010 is 28.8 mills, which is three percent higher than in 2009.

Counties received 51 percent of their total revenues in 2009 from property taxes, compared to 24 percent from GRT revenue. In contrast, municipalities received 70 percent of their revenue from GRT distributions and only nine percent from property taxes. Statewide, growth diminished over the last three years in almost all of the state's major revenue sources, except property taxes.

Mr. Maury discussed the lack of useful data available for state agencies to evaluate property tax issues. Certain data are provided to the TRD by each county assessor, but what is provided is usually insufficient. The TRD needs accurate individual data from each county, including assessed values, number of years of current ownership, when the properties sold, etc.

The committee recessed at 5:00 p.m.

<u>Tuesday, October 26</u>

The committee reconvened at 9:18 a.m. on Tuesday, October 26, 2010. The minutes from the August and September meetings of the committee were adopted without changes.

Manufacturing, Distribution and Logistics on the Border — PIT Credit

Juan Massey, director, regulatory affairs, Verde Realty, and Jerry Pacheco, vice president, Border Industrial Association, presented proposed changes in the law to expand PIT credits for residents of Texas who commute to New Mexico in the international border region. Currently, workers who work within 20 miles of the border with Mexico and are employed by certain manufacturing industries are allowed to be taxed at the rate that Texas imposes, which is currently zero. The new legislation proposes to expand eligible industries to include distribution and logistics businesses, and it changes the incentive into a PIT credit of up to $1,000 annually.

Mr. Pacheco said that this legislation is necessary because it is very difficult to get companies to relocate to the Santa Teresa area, from just across the Texas border, because of the PIT in New Mexico. Employees would prefer to stay in El Paso and not pay income taxes. In 2001, the legislature essentially exempted from the PIT workers commuting from Texas who work in the manufacturing industry. By expanding the exemption (now a credit) to the distribution and logistics industry, the Santa Teresa area stands to see a major surge in economic development.

Mr. Massey said that the new law would provide the PIT credit for 10 years; the maximum credit is $1,000, rather than unlimited; and companies using the credit would be required to increase their New Mexico employee payroll by 10 percent each year. He said that employee recruitment of New Mexico residents in the area has been challenging due to the high poverty rate, the lack of education of many residents and the lack of public transportation. He said that many distribution companies currently cross the international border at Santa Teresa and then drive into Texas to unload their product. The proposed legislation would attract large distribution companies to relocate to New Mexico.

Questions and comments from committee members included the following:

• Why bring in several hundred Texans to work in New Mexico businesses rather than provide education to the New Mexico work force? Mr. Pacheco said that training programs exist in the area, but there is a serious lack of qualified workers from New Mexico. He cited statistics that show that 37 percent of the potential workers in the area do not have a high school diploma.

• How will the credit help unemployed New Mexicans? Mr. Pacheco said that more time is needed to provide education and training to the local population. Companies using the credit would be required to increase their New Mexico work force by 10 percent each year.

• Instead of spending $1,000 per worker from Texas, why does the state not spend that money to provide better education to the New Mexico work force? Mr. Pacheco said that the PIT is the biggest obstacle in attracting Texas businesses to the Santa Teresa area.

• The legislature recently enacted a tax credit for train fuel, which benefited Verde Realty tremendously.

• The state needs tax policies that attract manufacturing businesses for the long term. Texas, facing a huge budget shortfall, will probably raise taxes, which will make New Mexico a more attractive business climate.

Use of Alternative Energy Tax Credits

Annie Carmichael, lobbyist, Sun Edison, reviewed the key tax policies in New Mexico that support solar energy development. Sun Edison is a global solar energy production and development company, with more than 380 plants in operation. The company focuses on retail and wholesale distributed generation, from roof-top generation facilities to large facilities producing many megawatts (MW).

A long-term, pro-solar-energy state policy is key to attracting companies like Sun Edison, said Ms. Carmichael. Property tax reductions, sales tax abatement and PIT and CIT solar production tax credits are the most common tax incentives that states provide to attract companies. New Mexico ranks very high among other states in solar energy incentives, and she encouraged the committee to keep those incentives intact.

Questions and comments from committee members included the following:

• What is the total dollar impact to the state of the new 50 MW facilities in southeastern New Mexico? Ms. Carmichael said that she will report that information to the committee. She estimated that 20 long-term jobs will be created once the construction phase is complete.

• What factors are limiting solar energy development in the state? Ms. Carmichael said that now that third-party financing is allowed for solar energy facilities, there really are no more obstacles.

• Sun Edison should obtain photovoltaic panels from New Mexico for its New Mexico projects.

Jet Fuel GRT Credit Sunset

Ed Mahr, lobbyist, Southwest Airlines, presented to the committee legislation to extend the current deductions from gross receipts and from compensating tax due for the sale of jet fuel in the state. Fifty-five percent of the value of the jet fuel is allowed to be deducted, and after July 1, 2012, the deduction amount is scheduled to be reduced to 40 percent. The proposed bill extends the 55 percent deduction level until 2017.

Southwest Airlines purchases jet fuel from three main sources, 40 percent of which is produced in New Mexico. The fuel is trucked and pumped through pipelines to Albuquerque from different locations. Mr. Mahr said that jet fuel is the second-highest expense of the airline, after personnel. Keeping the deduction at the 55 percent level will keep New Mexico somewhat competitive with other states. The airline industry is critical to the state's economy, he said.

Other options in addition to extending the sunset date for the jet fuel deduction would be to make the deduction 100 percent or to have no sunset of the deduction. The best option, however, would be to convert the GRT on jet fuel into a unit tax, based on volume rather than price. A unit tax would be much less volatile than the current GRT on the price of jet fuel.

Federal Low-Income Housing Credit Use in Valuation of Property

Steve Natelson, attorney, and Representative Gonzales presented legislation for the committee's consideration that would ensure that the value of federal affordable housing tax credits does not get calculated in the valuation of properties for property tax purposes. The New Mexico Mortgage Finance Authority (MFA) administers the federal tax credits, which are issued to property developers on a competitive basis. The purpose of the credits is to make the construction of low-income housing affordable; without the credits, it is not cost-effective to build most low-income housing.

Mr. Natelson represents the owner of an affordable housing project in Taos County who protested the valuation of the property by the county assessor. The county assessor attempted to value the property using the tax credit as a basis for valuation of the property. The TRD has never issued any regulatory guidance on this issue, and Taos County is the only county in the state to use such a valuation method. In addition, Section 7-36-15 NMSA 1978 requires the assessor to take into consideration the decrease in market value of an affordable housing property if it were to sell. This requirement, in essence, requires the assessor to factor in the rents charged to residents because federal law restricts the future use of those properties to affordable housing clients. The Taos County Valuation Protests Board ruled against the property owner, and the decision has been appealed to the district court. If the decision of the board stands and the new method of valuing affordable housing property spreads to other counties, there will be a chilling effect on affordable housing projects.

Questions and comments from committee members included the following:

• The committee should send a letter to the Property Tax Division of the TRD requesting that the division adopt a rule providing guidance to county assessors on this issue.

• Did the county assessor use rents in valuing the property? Steve Croiser, the developer of the property, said that the assessor used market-based rents, rather than the federally required contract rents, to determine the value of the property.

• Did Taos County provide land for the project, and how close was the MFA application estimate to the actual costs? Mr. Croiser said that the land was purchased at market value. In affordable housing projects, the return to the investor is generated by the federal tax credits. Valuing the property based on its replacement cost or potential sale cost does not work.

• What was the developer's original appraisal for the property? Mr. Croiser said he did not remember; he will provide that information to the committee. He said the total cost for the project was approximately $7 million. The annual income from the development is about $240,000. There are 56 units, and the average rent is $400 per month. Each year, the MFA develops an allocation plan, which determines project needs in each geographic area of the state. Developers then submit applications to the MFA for projects.

• Developers of low-income projects should not receive any special property tax treatment.

• How much do residents pay in rent? Representative Gonzales said that rents are determined based on family incomes. About 25 percent of the units at the development in Taos have rents provided by the federal government. Rents are typically $400 to $600 per month lower than full-market rent levels.

• County assessors in the audience were asked to comment on the correct method of valuation to use in affordable housing projects. Clyde Ward, county assessor, San Juan County, said that the three valuation approaches, sales of comparable properties, income and cost, are used. The cost approach and the income approach do not match up in this case, he said. Joaquin Valdez, county assessor, Los Alamos County, said that he uses all three methods of valuation and chooses the method that best suits a particular property. He said that Los Alamos County treats subsidized housing the same as regular housing properties.

• Why do county assessors have so much latitude in valuing properties? Mr. Natelson said that statute already requires county assessors to take into account the decrease in value of affordable housing projects. The Taos County assessor decided to use a brand new methodology to value those properties, without any statutory or regulatory authority.

Above-Ground Storage Tanks

Senator Sapien, Cyndee Biggers, petroleum distribution manager, Bowlin Travel Centers, and Scott Scanland, lobbyist, Bowlin Travel Centers, presented a bill to the committee that would provide CIT and PIT credits for 50 percent of the cost of complying with NMED requirements for upgrading above-ground fuel storage tanks. Senator Sapien said that he introduced Senate Bill 253 in the last regular legislative session to provide a similar credit for compliance.

Ms. Biggers said that Bowlin Travel Centers operates seven facilities. Two of those facilities have ceased providing gasoline to retail customers because the company determined that the cost of compliance with NMED rules is too high. The NMED has mandated that storage tanks be double-walled or that secondary collection areas be installed according to NMED specifications. The company has completed upgrading one facility, at a cost of $120,000. The department has set a July 1, 2011 deadline for facilities to comply with the rule. She asked the committee to support the legislation, which would partially offset the cost of compliance.

Ruben Baca, executive director, Independent Petroleum Marketers Association, said that complying with the new rule has been a problem for many companies. Of the 1,300 above-ground storage tanks in the state, only 300 are currently in compliance.

Mr. Scanland said that the NMED rules are a huge unfunded mandate. Many of these tanks were installed in order to comply with previous stricter rules governing underground storage tanks at significant expenses to the property or business owners. Now they are being asked to upgrade those new tanks at an additional and considerable expense. It would be easier to allow the owners to allow the new tanks to remain for their life and change to the newer provisions when replacement of the tanks becomes necessary.

Senator Sapien said that there are many small businesses that cannot afford the cost of compliance, and they will be forced out of the business of selling gasoline.

Questions and comments from committee members included the following:

• Instead of providing a tax credit, the legislature should enact a moratorium on the storage tank rule.

• What is the estimated fiscal impact on the state of the credit? Senator Sapien said that it will cost the state $6 million, which will probably be offset by the tax revenue the state will receive if these businesses continue to operate.

• New tax credits are difficult to justify in the current economic downturn. The NMED rule should be repealed instead.

• Some state agencies have overly broad statutory authority to adopt rules. Mr. Baca said that New Mexico is the only state in the nation that regulates above-ground storage tanks.

• The Government Restructuring Task Force will probably endorse a bill that gives the legislature the ability to review agency rules.

• In 1989, the legislature provided that a portion of the proceeds of the petroleum products loading fee be deposited into the Corrective Action Fund to help with the costs associated with replacing underground storage tanks. However, the legislature recently enacted a law that redirected that portion of the tax for other purposes. This distribution should be used to help with the compliance costs of the above-ground storage tank rule. Mr. Baca said that redirecting the tax would provide about $6 million annually.

• Maybe the NMED rule should be amended to require double-wall tanks on new installations only.

There being no further business, the committee adjourned at 3:22 p.m.

REVENUE STABILIZATION AND
TAX POLICY COMMITTEE

Section 8

November 2010
Agenda
Minutes

Revised: November 23, 2010

TENTATIVE AGENDA
for the
SIXTH MEETING IN 2010
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

November 29-30, 2010
Room 322, State Capitol

Monday, November 29

9:00 a.m.	**Call to Order** —Representative Edward C. Sandoval, Chair
9:05 a.m.	**Penalty Assessment Remittance — Agency Change** —Patrick Simpson, Deputy Director, Administrative Office of the Courts
10:00 a.m.	**Tourism Marketing Tax Proposal** —Michael Cerletti, Secretary of Tourism
11:00 a.m.	**Tax Proposals** —Senator Timothy M. Keller
12:00 noon	**Lunch**
1:45 p.m.	**County and Municipal Utility Right-of-Way Fees** —Tito Chavez, Consultant, New Mexico Association of Counties (NMAC) —Harold Garcia, Chair, NMAC Public Works Affiliate —Doug Moore, Chair, Otero County Commission —Scott Krahling, Commissioner, Dona Ana County Commission —Dan Bryant, County Attorney, Otero County
2:45 p.m.	**Unemployment Trust Fund Solvency — Issues and Options** —Kenneth Ortiz, Secretary of Workforce Solutions
3:45 p.m.	**New Mexico Municipal League Legislative Priorities** —William Fulginiti, Executive Director, New Mexico Municipal League
4:30 p.m.	**Electric Car Gross Receipts Tax Credit**

—Representative Jim R. Trujillo

5:15 p.m.	**Recess**

Tuesday, November 30

9:00 a.m.	**Reconvene** —Representative Edward C. Sandoval, Chair
9:05 a.m.	**City of Las Cruces and Mesa Del Sol and TIDD Updates** —Sen. Mary Kay Papen —Larry Horan, Lobbyist, City of Las Cruces —Mike Daly, President, Mesa del Sol —Tom Horan, Lobbyist, Mesa del Sol
10:05 a.m.	**Necessary Tax Deductions and Exemptions Distinguished from Tax Expenditures** —Tom Clifford, Chief Economist, Legislative Finance Committee
11:05 a.m.	**Cable Television Update** —Susan Bitter Smith, Executive Director, Arizona-New Mexico Cable Communications Association —Scott Scanland, Lobbyist, Arizona-New Mexico Cable Communications Association
12:05 p.m.	**Lunch**
1:20 p.m.	Tax Incentive Discussion —Pam Ray, Staff Attorney
2:30 p.m.	**Adjourn**

MINUTES
of the
SIXTH MEETING IN 2010
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE
November 29-30, 2010
Room 322, State Capitol
Santa Fe

The sixth meeting of the Revenue Stabilization and Tax Policy Committee (RSTP) for 2010 was called to order by Representative Edward C. Sandoval, chair, on Monday, November 29, 2010, at 9:18 a.m. in Room 322 of the State Capitol in Santa Fe.

Present
Rep. Edward C. Sandoval, Chair
Sen. John Arthur Smith, Vice Chair
Sen. Carlos R. Cisneros
Rep. Nathan P. Cote
Rep. Anna M. Crook
Sen. Tim Eichenberg
Rep. Keith J. Gardner (11/29)
Sen. Timothy Z. Jennings, President Pro Tempore (11/29)
Sen. Timothy M. Keller
Sen. Gay G. Kernan
Rep. Ben Lujan, Speaker of the House (11/30)
Rep. Rodolpho "Rudy" S. Martinez
Sen. Howie C. Morales
Rep. Henry Kiki Saavedra
Rep. Thomas C. Taylor
Rep. Jim R. Trujillo

Absent
Sen. Dianna J. Duran
Sen. William E. Sharer

Designees
Rep. Miguel P. Garcia (attending as a guest 11/30)
Sen. Phil A. Griego (attending as a guest)
Sen. Clinton D. Harden, Jr.
Sen. Nancy Rodriguez (attending as a guest)
Rep. Luciano "Lucky" Varela (attending as a designee 11/29 and as a guest 11/30)

Rep. Ray Begaye
Sen. Mark Boitano
Rep. Donald E. Bratton
Rep. Zachary J. Cook
Sen. Kent L. Cravens
Rep. Roberto "Bobby" J. Gonzales
Rep. Sandra D. Jeff
Sen. Carroll H. Leavell
Rep. Antonio "Moe" Maestas
Sen. Steven P. Neville
Rep. Debbie A. Rodella
Sen. Bernadette M. Sanchez

Sen. John M. Sapien
Rep. James R.J. Strickler
Rep. Don L. Tripp
Sen. Peter Wirth

Guest Legislator Attending
Sen. Cisco McSorley (11/29)

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

Staff
Pam Ray, Legislative Council Service (LCS)
Doris Faust, LCS
Ric Gaudet, LCS

Monday, November 29

Penalty Assessment Remittance — Agency Change

Patrick Simpson, deputy director, Administrative Office of the Courts (AOC), presented proposed legislation for the committee's consideration to change the process of administering traffic citations. The bill eliminates the requirement that motorists cited for a violation of traffic laws decide immediately whether to plead guilty or to contest the citation. Instead, motorists will have 30 days to either contest the citation or pay the fine. The bill also specifies that all fines and fees are to be paid to the AOC. Currently, uncontested citation fines and fees are paid to the Motor Vehicle Division (MVD) of the Taxation and Revenue Department (TRD), and contested citation fines and fees are paid to the AOC. The change will streamline the process of administering traffic citations, and it will relieve the MVD of those responsibilities. Magistrate and metropolitan court staff will see an increased workload from the change, so the bill creates a new traffic citation fee of $10.00, which will provide for additional staff at the courts. The MVD does not collect any money from the administration of traffic citations but funds the program through its general appropriation act budget. Mr. Simpson estimated that the magistrate courts will process 173,000 additional uncontested citations each year.

Questions and comments from committee members included the following.

- There are already too many fees that are added to a traffic citation. The proposed traffic citation fee is essentially a new tax that will fund government programs. Mr. Simpson said that the TRD supports the legislation, and it will reduce the workload of the MVD.

- The current structure of earmarking penalty assessment fees should be changed so that all fees are deposited into the general fund and the programs are funded yearly by the legislature.

- How will the revenue generated from the new fee be used? Mr. Simpson said that the money would be distributed to magistrate and metropolitan courts for the administration of traffic citations.

- The TRD budget should be reduced to account for its reduced workload if the legislation is enacted.

- Why does the bill give the AOC the ability to modify the uniform traffic citation form? Mr. Simpson said that the AOC wants to have more input into the citation form. Some changes made to the form in the past have not worked well for the AOC.

- How much money in fees is currently collected for a traffic citation from Section 35-6-1 NMSA 1978 versus Section 66-8-116.3 NMSA 1978? Mr. Simpson said that a person who is found guilty in contested cases, pursuant to Section 35-6-1 NMSA 1978, pays a total of $76.00 in the magistrate court and $80.00 in the metropolitan court. The total fees paid pursuant to Section 66-8-116.3 NMSA 1978 for uncontested citations is $61.00 in counties with a magistrate court and $55.00 in counties with a metropolitan court.

- The section in the proposed bill creating the traffic citation fund needs to specify that money in the fund can only be spent pursuant to legislative appropriation.

- Representatives of the MVD and magistrate courts should have appeared before the committee. Mr. Simpson said that the AOC represents magistrate courts. He said that the MVD is in favor of the change. The MVD currently has 20 full-time-equivalent (FTE) employees who administer all fees, fines and registrations included in the Motor Vehicle Code.

- This restructuring bill should have been presented to the Government Restructuring Task Force. Fern Goodman of the AOC said that the judiciary did present the idea of switching the administration of traffic citations from the MVD to the magistrate courts. However, the proposal was still in the development phase and was not in bill form.

- The $10.00 fee for each traffic citation will generate more money than needed for the magistrate courts. Where will the extra money be distributed? Mr. Simpson said that some magistrate courts will need additional personnel to manage the increased workload. Statewide, there may be a need for 10 to 20 additional FTEs, but the impact on the courts is still uncertain. Magistrate courts have already made large budget cuts in the past two fiscal years, and any more cuts will result in employee furloughs. While the proposed legislation will end up making the administration of traffic citations more efficient, magistrate courts will need additional revenue to implement the program. Money generated from the traffic citation fee will not be spent on AOC staff raises or other perks.

- The municipal penalty assessment program, commonly referred to as "red-light camera citations", that diverted money from magistrate courts to municipalities should be stopped. Traffic citations should not be a revenue source for municipalities.

Tourism Marketing Revenue Proposals

Secretary of Tourism Michael Cerletti and Deputy Secretary of Tourism Jennifer Hobson discussed with the committee several options for providing a dedicated revenue stream for the advertising program of the Tourism Department (TD). Secretary Cerletti began by reviewing the economic impact tourism has in New Mexico. Tourism spending in 2008 generated $6 billion in economic activity in the state and $765 million in federal, state and local tax receipts. The state realized $370 million in revenue from tourism in 2008, which accounts for about seven percent of general fund revenues. The department is underfunded; New Mexico ranks thirty-second in the nation in tourism advertising spending.

Ms. Hobson presented four options for providing a dedicated revenue stream for the TD.

- Redirect the $2.00 daily surcharge levied on rental car operations from the general fund to the TD budget. The $4.5 million generated by the surcharge each year would replace the $3 million general fund operating budget the department currently has.

- Dedicate 50 percent of any increase in Indian gaming revenue-sharing payments above fiscal year 2010 levels for the department.

- Enact a surtax of .25 percent of restaurant sales, which would be dedicated for TD advertising programs. The surtax would raise an estimated $6.5 million each year.

- Dedicate 3.5 percent of the average Severance Tax Permanent Fund yearly distributions, which would generate approximately $6.3 million each year.

Questions and comments from committee members included the following.

- The TD needs more advertising funding, but the money should be appropriated from the general fund rather than being earmarked from a particular source. Secretary Cerletti said that tourism is one of the top three industries in 49 states. Advertising funding has been cut 22 percent in the past few years, which has had a small negative impact on the number of tourists visiting New Mexico. Art Bouffard, president of the New Mexico Lodging Association, said that the past few years have been difficult for the lodging industry but occupancy rates are starting to increase. Martin Leger, advertising director, TD, said that several years ago, Colorado eliminated its tourism advertising budget and subsequently suffered tourism-generated revenue declines of 35 percent. He cited recent studies that found that for every $1.00 spent on tourism advertising, the state realizes $40.00 in economic activity.

- Does the state get any revenue from the occupancy tax? Secretary Cerletti said that all money generated by the tax is used by the local governments imposing the tax. He said the current structure of the tax is a good policy, and he recommended that distribution of its revenues not be changed.

- Has the New Mexico Restaurant Association (NMRA) endorsed the restaurant sales surtax idea? Allison Smith, government affairs director, NMRA, said that the association endorsed that idea in 2009 but has not considered endorsing the legislative proposal in 2010. The association is investigating other methods of raising tourism advertising revenues, she said.

- State money spent on public museums should be more fairly distributed around the state, which will increase tourism to those areas that currently receive no funding. Secretary Cerletti said that he expects that the opening of Spaceport America will be a tremendous boon to the tourism industry in the Las Cruces area. Ms. Hobson said that the TD has made an effort to advertise parts of the state besides the north-central region. She mentioned ecotourism promotions related to space tourism at the spaceport.

- When Colorado cut its tourism funding, rural areas and small businesses around the state suffered.

- How do New Mexico's occupancy tax rates compare to lodger's tax rates in the surrounding states? Mr. Bouffard said that the occupancy tax rate varies between three percent and seven percent, depending on the municipality. He said that if the total of the occupancy tax rate and the gross receipts tax (GRT) rate gets much higher than 13 percent, tourism revenues tend to decline in that area. Santa Fe's combined rate is above 15 percent, he said.

- Would the casino revenue-sharing agreements with tribes need to be amended in order to dedicate revenue toward tourism advertising? Mr. Leger said that the agreements only specify the amount tribes pay to the state, not how the state spends the money.

- Does New Mexico spend tourism advertising money promoting tribal casinos? Secretary Cerletti said that all TD advertising is generic. The presence of casinos is sometimes used as a method of attracting tourists, depending on the intended audience.

- Earmarking revenues is not a sustainable revenue source. The state needs to ensure that all entities pay some taxes, which will allow for more revenue for tourism advertising and other important state programs.

Tax Proposals

Senator Keller presented three proposed bills for the committee's consideration.

Tax Expenditure Budgets

This legislation would require the TRD to prepare annually a tax expenditure budget, tracking the costs and benefits of tax incentives and other credits, rebates, deductions and exemptions. The budget would include a projection of the costs of tax expenditures for all significant general fund revenue sources; the statutory basis for each expenditure; the amount of revenue the state forgoes for each expenditure; the beneficiaries of each expenditure, including the number of jobs created; and any significant unintended consequences of each expenditure. The proposed bill is nearly identical to the bill that passed both houses of the legislature almost unanimously in 2007 but was vetoed by the governor.

Questions and comments from committee members included the following.

- How would film production tax credit reporting have been different had this bill become law in 2007? Senator Keller said that much better information about the credit would have been available.

- What is the fiscal impact of the legislation? Senator Keller said that the 2007 fiscal impact report (FIR) estimated the tax expenditure budget would cost $100,000 annually. However, the TRD this year produced, in-house, a report that is essentially a tax expenditure budget, but for much less money.

- A tax expenditure budget will need to detail the tax expenditures granted to nonprofit entities, as well as to businesses. Senator Keller said that this legislation, coupled with another bill he is proposing to require specific reporting of all deductions and exemptions, will ensure that data be collected.

- The state needs to perform dynamic economic modeling of tax expenditures in order to measure the indirect impacts and forgone opportunities of those expenditures. Senator Keller agreed, but he said that kind of study is expensive. The legislation he is proposing requires reporting of many specific indicators but does not require dynamic studies.

- How will the number of jobs created be measured accurately? Senator Keller said that there is still a policy question of which state agency should develop the tax expenditure budget. The agency would use a standardized formula using existing methodologies to determine the number of jobs created.

- State agencies need the ability to share confidential information. Senator Keller said that a bill to allow sharing of confidential information was vetoed in 2009.

<u>Film Production Tax Credit Act</u>

The proposed bill would provide better tracking requirements for companies claiming the film production tax credit. Key provisions of the legislation include requirements for tracking the return on investment of the credit; the development of a standard form for reporting; the requirement that film production companies waive certain confidentiality provisions in order to receive the credit; providing for a five-year review and sunset of the legislation; and compiling existing statutes relating to the credit into a new "Film Production Tax Credit Act". Film production companies would be required to report the number of jobs created and total wages paid in New Mexico; the number of New Mexico residents employed; the total amount of GRT paid; and other information the TRD and the Economic Development Department determine to be necessary to evaluate the effectiveness of the credit.

Questions and comments from committee members included the following.

- Does the film production tax credit currently have sunset provisions? Senator Keller said the tax credit is permanent.

- The state provides no-interest loans to film production companies. Can a company get a loan from the state and qualify for the tax credit? Senator Keller said that there is nothing in statute prohibiting a company from receiving both incentives.

Itemization of GRT Deductions and Exemptions

The proposed legislation would direct the TRD to revise GRT and compensating tax forms to require taxpayers to itemize exemptions and deductions on those forms. Currently, the TRD cannot accurately quantify deductions and exemptions because they are not reported separately.

Questions and comments from committee members included the following.

- How will this legislation affect businesses? Senator Keller said that businesses already have to quantify each deduction they are claiming, but then they merely report the total of all deductions claimed. The new legislation will not cause any hardships because businesses are not required to do any more work, except to list the deductions individually.

- Senator Keller was asked to review the legislation with tax accountants for any potential problems before introducing the bill.

County and Municipal Right-of-Way Fees

The committee heard a presentation from a panel of county officials about the ability of counties to impose right-of-way (ROW) fees on public utilities for the use of those easements. Panel members included Tito Chavez, former state senator and consultant, New Mexico Association of Counties (NMAC); Harold Garcia, public works director, San Miguel County, and chair, NMAC Public Works Affiliate; Doug Moore, chair, Otero County Commission; Scott Krahling, commissioner, Dona Ana County Commission; Larry Moore, Quay County road supervisor and vice chair, NMAC Public Works Affiliate; Dan Bryant, county attorney, Otero County; Paul Gutierrez, executive director, NMAC; and Tasia Young, lobbyist, NMAC.

Mr. Garcia said that the NMAC Public Works Affiliate convened a ROW committee in order to address the problem created when the Public Regulation Commission (PRC) questioned the validity of existing ROW agreements between counties and utility companies. The PRC ruled that the agreements were not valid because they had not been reviewed by the commission. The decision of the PRC was appealed to the New Mexico Supreme Court, which overturned the PRC's decision. The ROW committee has been studying the issue of how to clearly establish statutory authority for counties to enter into ROW agreements with utility companies.

County roads are often damaged when utility companies access their infrastructure that is located under the roads. Some counties have entered into agreements with the companies as a means of offsetting the damage to county roads. Municipalities have clear statutory authority to enter into these agreements; however, a county's authority to do so is more vague.

Mr. Moore said that Otero County had been collecting ROW franchise fees since 1987, until recently when the PRC decided those agreements were not valid. Utility companies need to be charged for the damage they do to county roads; if not, then the county may be subsidizing utility companies, in possible violation of the anti-donation provisions of the Constitution of New Mexico. Mr. Krahling said that county officials want to formalize, in statute, the right of counties to enter into ROW agreements. Mr. Chavez said that the ROW committee has had three meetings with utility companies and municipalities, and the only remaining issue to resolve is how to establish fee structures for electric cooperatives and large industrial energy users. Mr. Bryant explained that the ROW committee is working on language to reflect the fact that many cooperatives do not use ROW easements on public roads, so they should not be subject to ROW fees.

Questions and comments from committee members included the following.

- Are counties trying to get the authority to grant new ROW easements? Mr. Bryant said that counties already have that authority; what they are seeking is the ability to recoup expenses from damage to county roads.

- Many county roads do not have written ROW easements; instead, counties often used prescriptive easements to make existing roads into county roads. Counties then granted ROW easements to utility companies through those roads, which may have violated the landowners' property rights. If a county cannot maintain a county road, it should deed the road back to the owner of the property. Mr. Moore said that county commissions have the legal authority over county roads. Otero County only gets $.05 per mile from the state, and it is charged with maintaining 1,600 miles of county roads. Utility companies often do shoddy work when accessing their infrastructure, leaving damaged roads as well as liabilities for the county if utility infrastructure is later damaged by road maintenance. He cited an example of a telephone company installing a high-speed phone cable only 14 inches below the ground.

The following year, heavy rains washed out portions of the road, and a county road grader damaged the cable, for which the phone company demanded restitution.

- Instead of granting counties the authority to charge fees to utility companies, counties might need stronger enforcement capabilities to ensure that utilities meet quality standards.

- Can a county deny a utility access to its underground infrastructure? Mr. Bryant said that counties do not have the authority to deny ROW access to a utility company.

- Questions were raised about the locations of ROW committee meetings and whether all interested parties were included in the discussions. Mr. Gutierrez said that the NMAC Public Works Affiliate has representatives from all counties. The ROW committee will propose the recommended legislation to the full NMAC board for its consideration. If the board approves the idea, then each county representative will present it to individual county commissions. He said that the legislation will include the option for counties to opt out of entering into ROW agreements.

- Could the ROW fee be based on the number of miles of road used by a utility company, rather than a percentage of revenue? Mr. Chavez said that idea could work, except that it would be challenging to determine actual mileage.

- If counties get a fee from utility companies for ROW access, landowners should also receive some of that revenue.

- Counties have the ability to assess road maintenance fees, yet they are reluctant to raise taxes. Mr. Moore said that utility companies need to pay for the damage they cause to public roads; it would not be fair to tax county residents in order to pay for that.

Unemployment Trust Fund Solvency — Issues and Options

Secretary of Workforce Solutions Ken Ortiz discussed with the committee the solvency of the Unemployment Insurance Trust Fund (UITF) account of the Unemployment Compensation Fund. The UITF, which provides unemployment compensation, is projected to become insolvent by August 2011 unless some action is taken. Proactive steps were taken in fiscal year 2010 to maintain the UITF's solvency, but the 500 percent increase in unemployment benefit claims in the past 30 months has meant that the UITF will soon be unable to cover unemployment liabilities. The legislature recently transferred $117 million to the UITF from another state government unemployment trust fund; decreased the average weekly compensation from 60 percent to 53.5 percent; and increased the employer contribution levels, beginning in January 2011.

Without congressional action to fund extended unemployment benefits, the UITF balance will fall below zero in August 2011, assuming the unemployment rate remains constant at 8.4 percent. The federal extended benefits were scheduled to expire the following day, November 30, 2010, which meant that federal unemployment compensation tiers 1-4 will no longer be available. After that date, total benefits for new claims will be reduced from 93 weeks to 46 weeks in New Mexico, and the state will begin paying 50 percent of extended benefits beyond the regular benefit period of 26 weeks. In the worst case scenario, UITF insolvency will result in a mandatory loan from the United States Department of Labor, the automatic changing of employer contributions from level 1 to level 6 and the loss of a federal tax credit for employees. The employer contribution change will result in an average payment per employee of $512 per year, which would be more than a 200 percent rate increase.

Secretary Ortiz presented potential cost savings and revenue enhancements that the legislature could consider. He said that the Workforce Solutions Department (WSD) is not advocating any particular change because those policy decisions need to be made by the next administration. New Mexico has several additional unemployment benefits that add $71 million annually to the cost of the program, including extended/high unemployment period benefits; full-time student benefits; dependent allowance benefits; part-time work allowances; alternate base period calculations; military spouse benefits; and domestic violence benefits. Revenue enhancement options include increasing the employer contribution rate schedule; increasing the rate for new employer contributions; imposing a short-term surcharge on employers; and increasing penalties for delinquent filers.

Questions and comments from committee members included the following.

- How do the part-time work benefits function? Secretary Ortiz said that the people who are receiving unemployment compensation benefits and subsequently start working part time receive reduced benefits, rather than having their benefits terminated.

- Can a person receiving retirement benefits also receive unemployment compensation benefits? Clyde DeMersseman, general counsel, WSD, said that current law allows unemployment compensation benefits to be paid, but those payments are reduced according to the pension amount. However, the WSD can only act on information provided to the department, and some claimants do not inform the department that they are receiving pensions or other income.

- A few years ago, the UITF had a huge surplus, so the legislature froze the employer contribution rate at schedule 0.

- How do extended-week benefits work? Secretary Ortiz said that basic benefits are for 26 weeks, fully paid for by the state. There are four tiers of federal benefit level extensions, which are triggered based on the state's unemployment level. Those federal extensions have been funded completely by the federal government, but the state will begin paying 50 percent of those benefits December 1, 2010, unless Congress authorizes more funding at the federal level.

- Unemployment compensation benefits should not be paid to people who fail a drug test. Mr. DeMersseman said that some states have attempted to implement that idea, but courts have ruled against that approach. An alternate possibility would be to condition benefits on "readiness to work", which could be defined as being drug-free.

- Will reductions in the additional benefits help the solvency of the fund? Secretary Ortiz said that the additional benefits, other than extended-week benefits, account for less than 10 percent of total annual expenditures from the fund. Cuts in those areas could help, but they have been identified as socially important or economically beneficial. The domestic violence benefit, while not being an economic development tool, only costs $162,000 and provides benefits to people who are forced to quit their jobs due to domestic violence issues.

- Would a college instructor who teaches two semesters of courses be eligible for benefits during the summer months? Mr. DeMersseman said that educational employees are treated differently from employees of most other industries. An individual's "attachment to the workforce" is considered before benefits are granted. Thus, a college instructor would have a reasonable expectation of being rehired and would not be eligible for benefits.

- Would military retirees who move to another state be eligible to collect unemployment compensation benefits? Mr. DeMersseman said that federal regulations for military retirees are different than for other industries. He will research that question and report back to the committee.

New Mexico Municipal League Legislative Priorities

Bill Fulginiti, executive director, New Mexico Municipal League (NMML), discussed with the committee the league's priorities for the upcoming legislative session. Rather than asking for legislation to be enacted, Mr. Fulginiti said the NMML is asking that the state not enact any legislation that would result in the loss of municipal revenues or any legislation that would preempt the ability of municipalities to tax certain transactions. He reminded the committee that, on average, 75 percent of all municipal revenues are derived from the GRT, and the recent economic recession has hurt municipalities. GRT revenue declines have ranged from one percent to 39 percent. The City of Belen has laid off 25 percent of its city employees and is still facing a $3.8 million shortfall. The City of Albuquerque has a $66 million deficit, which is about eight percent of the city's general fund budget.

If the legislature enacts a law to repeal the "hold-harmless" provisions in statute, designed to protect city revenues from the gross receipts deduction allowed on food, municipalities will be faced with an even greater budget shortfall. That change would result in a loss of revenues to Albuquerque of 8.8 percent, and to Hatch of 30 percent.

Questions and comments from committee members included the following.

- Has there been any congressional movement on the issue of taxing internet sales? Mr. Fulginiti said that, unfortunately, online companies have been essentially purchasing congressional members in order to stall that legislation.

- Albuquerque still has unused GRT taxing authority. Every entity in the state needs to share in the pain of budgetary shortfalls, and the hold-harmless provisions need to be revisited. Municipalities were the recipients of a revenue windfall a few years ago when fiscal projections of the GRT food deductions were incorrect. Mr. Fulginiti said that municipal GRT increases have to be approved by the voters, which is not always easy to do. When food was part of the GRT base, the revenues generated by the GRT had been pledged to the payment of revenue bonds. The hold-harmless provisions ensured the bonds' repayment, which had been guaranteed by the state in statute. If the state removes the protection of those bonds, bond-rating agencies will reduce the state's bond ratings, which will cost state and local governments far more money than the hold-harmless provisions currently do.

- Will cities benefit if the GRT is reimposed on food? Mr. Fulginiti said that the legislature passed in 2010 a bill to have a local option GRT on food, which legislation would be acceptable to municipalities. The governor repealed that legislation, however.

- Taxing food purchases of low-income people is a regressive tax policy, but most middle- and high-income people should pay the GRT on food.

- How did the vetoed distribution of cigarette tax revenues to municipalities happen? Mr. Fulginiti said that when the cigarette tax rate was raised in 2010, the distribution of the tax to various existing recipients was also changed to reflect the tax rate change. Although the distribution to municipalities had been in statute for years and was not being substantively modified, the governor deleted the entire distribution from the act. Mr. Fulginiti said that municipalities were very surprised at the line-item veto.

Electric Car Tax Credit

Representative Trujillo and Murray Thompson, lobbyist, General Motors (GM), presented a proposed bill that would grant a one-time exemption from the motor vehicle excise tax from the sale of qualified electric plug-in electric drive vehicles. The tax credit would be available from 2011 to 2014. Mr. Thompson said that the Chevrolet Volt, which is expected to be on the market in 2011, is the first of the next generation of alternative energy vehicles. A fiscal impact report has not yet been prepared for the legislation, but last year, it was estimated that it would cost $1.5 million annually. GM will manufacture 10,000 of these cars in 2011, and 30,000 in 2012.

Questions and comments from committee members included the following.

- How much will the Volt cost? Mr. Murray said the base price for the car is $41,000. It has a top speed of 100 miles per hour.

- Inversely indexing the amount of the tax credit to the price of gasoline would have the effect of stimulating car sales through tax incentives when gas prices are low, but when gas prices are high, natural market forces will have the same sales effect without the need for this credit.

The committee recessed at 5:30 p.m.

Tuesday, November 30

The committee was reconvened at 9:17 a.m. on Tuesday, November 30, 2010, by Representative Sandoval.

City of Las Cruces and Mesa del Sol Tax Increment Development District Updates

Senator Mary Kay Papen; Larry Horan, lobbyist, City of Las Cruces; Mike Daly, president, Mesa del Sol; and Tom Horan, lobbyist, Mesa del Sol, gave an update of two tax increment development districts (TIDDs) in the state. Senator Papen sponsored legislation authorizing the City of Las Cruces Main Street Downtown TIDD to receive the state portion of GRT revenues realized from extra economic activity in the TIDD. She said that the Las Cruces TIDD will be beneficial to the city and will create jobs in the area. Larry Horan said that the TIDD has just received the first increment from the state, which has amounted to $1.8 million. Most of the economic activity from the district has been from the reconstruction of Main Street and from work on the Rio Grande Theater. He estimated a net gain of 200 jobs from the projects. The city has completed construction of a new city hall and is currently looking for tenants for the old building. Private development is beginning to occur in the area, and the farmers' market has brought many residents downtown to shop.

Mr. Daly updated the committee on the Mesa del Sol TIDD, which was created in 2006. The legislature in 2007 authorized up to $500 million in bonding capacity over 25 years from economic activity in the district. Mesa del Sol receives tax increment dedications from the state, the City of Albuquerque and Bernalillo County. The first bonds were issued in October 2009, with $3.6 million being reimbursed for public infrastructure. Current commercial tenants include Albuquerque Studios, Fidelity Investments, Schott Solar, Molina Healthcare, MSR-Fraunhofer, the Aperture Center and the federal Drug Enforcement Agency and Immigration and Customs Enforcement. Mesa del Sol has built a school for an international baccalaureate charter elementary school, which is the first of its kind in the state. All of the green space areas of the development used locally grown plants, and recruitment programs in the South Valley of Albuquerque have resulted in 25 people being hired by Mesa del Sol's businesses. Finally, Mr. Daly said that his company has invested $80 million into Mesa del Sol, and it is here to stay. The company has not earned a profit yet, but he expects that milestone will be passed in the near future.

Questions and comments from committee members included the following.

- How much does land cost in the development? Mr. Daly said that Mesa del Sol started selling land at $2.50 per square foot but needs to reach $5.00 per square foot in order to become profitable. He compared the price of land at Mesa del Sol to other developments with much higher land prices.

- When will residential development begin? Mr. Daly said that he expects construction to begin in 18 months. He said that he believes the residential real estate market will not recover until 2014.

- Does Mesa del Sol provide state office space for free? Mr. Daly said that staff for the state's supercomputer has been provided free space until the building finds a commercial tenant.

- What is the status of potential new interchanges on Interstate 25? Mr. Daly said that $20 million in state funding and $2 million in Mesa del Sol funding have been allocated for a new interchange.

- The charter school will be open to all Albuquerque Public Schools (APS) students, so transportation could be an issue. Additionally, residents of Mesa del Sol will not have any enrollment preference. Mr. Daly said that the law requires that charter schools be open to all students in a district. There will eventually be a regular public school in the area, but until then, Mesa del Sol has agreed to pay APS $3,000 in impact fees for every student in the development attending an APS school.

- Mesa del Sol has done a great job of economic development. The news media have unfairly portrayed TIDDs as draining resources from developed areas to new developments.

Necessary Tax Deductions and Exemptions Distinguished from Tax Expenditures

Tom Clifford, chief economist, LFC, discussed tax expenditures in statute and how they could be evaluated. He began by reviewing the LFC's adopted good tax policy principles of adequacy, efficiency, equity, simplicity and accountability, and he mentioned that targeted expenditures like tax incentives necessarily conflict with the simplicity principle. Tax expenditures, broadly defined, are revenue losses from tax provisions that grant special relief designed to encourage certain kinds of behavior or to aid taxpayers in special circumstances. Advantages of using tax expenditures to affect policy include the ability of using an existing government system to target expenditures and the relative ease of gathering information to be able to accurately target the expenditure. Disadvantages include their inherent inequity, complexity and lack of transparency and the lack of control by policymakers over their budgetary impacts.

Mr. Clifford categorized 96 tax expenditures found in New Mexico statutes. Economic development incentives will cost the state $104.6 million in fiscal year 2012 general fund revenues; anti-poverty, health and education incentives will cost $367.5 million; renewable energy incentives will cost $24.5 million; and other incentives will cost $444.5 million.

Economic development incentives include the film production tax credit, which is estimated to cost $70 million this year; the investment credit, costing $7 million; the technology jobs tax credit, costing $6.6 million; and the high-wage jobs tax credit, costing $5.6 million. Economic development incentives provide targeted relief to encourage businesses to start up in or relocate to New Mexico and may cover up other deficiencies the state may have in attracting businesses. However, many of these incentives lack accountability and reporting requirements, and the complexity of some incentives may actually undermine their effectiveness.

Health care expenditures cost the state $220 million and mostly consist of the insurance premium tax credit for $77 million, the GRT deduction from managed care services for $75 million, the GRT prescription drug deduction for $19 million and hospital credits and deductions for $23.5 million. Although health care tax credits may be intended to improve health care delivery in the state, the uneven treatment of the credits is not fair to large segments of the population. Since one-third of the state's revenues is spent on the health care sector, exempting large portions of that industry from taxation may compromise the adequacy of state revenues.

Anti-poverty incentives include the working families tax credit, which will cost $45 million; the exemptions from income taxation of low- and middle-income households, which cost $30 million; the low-income comprehensive tax rebate, which costs $24 million; and the federally mandated exemption from the GRT on food stamps, which costs $20 million. Although targeting of relief can easily be achieved through the tax system, some forms of targeting may not actually benefit the intended recipient. Administrative costs may also outweigh some of the benefits. Mr. Clifford said that although the overall tax system in New Mexico is regressive, state spending is progressive.

Renewable energy incentives include various energy production credits, costing $20 million, and a GRT deduction for wind energy equipment, costing $2 million. Issues with renewable energy incentives include that the tax system is an inefficient system to administer these complex incentives; the public benefits of renewable energy are not quantifiable; the layering of various incentives means that large subsidies are being offered to the industry; and sunsetting provisions will be needed to prevent erosion of the tax base if the industry grows larger.

Other tax expenditures include the deduction of food receipts from the GRT, which will cost $217 million; the cigarette tax exemption for tribes, costing $75 million; the oil and gas emergency school tax royalty deduction, costing $40 million; the deduction from income tax of capital gains, costing $37 million; and certain insurance company receipts not being taxed at all, costing $26 million. Concerns with some of these expenditures include that some expenditures, like the food deduction, do not benefit low-income households. The cumulative revenue impact of these tax expenditures also raises adequacy concerns.

Mr. Clifford then described "normal" exemptions and deductions, which, for various reasons, are necessary but would not be considered tax expenditures or incentives. Some exclusions are designed to prevent double taxation on items such as investment income, wages, dividends, motor vehicles, most oil and gas activities and fuel. Other exclusions are designed to prevent pyramiding of the GRT, including many business-to-business transactions, agricultural products, commissions, sales for resale and energy used in production activities. Other activities have been excluded from the tax base, including sales by governments, some sales of nonprofit entities, pass-through entity income exclusions and activities preempted by federal law from taxation.

Mr. Clifford then discussed various tax rate differentials, which could be considered tax expenditures or disincentives. While the average GRT rate in New Mexico is seven percent, other taxes that involve sales range between one percent and 30 percent. There are often mitigating reasons for the differentials, such as additional taxes paid by the industry, but the legislature should periodically study those issues to ensure that the tax system is equitable. Finally, Mr. Clifford discussed accountability provisions that should be considered, including tax expenditure reports that include detailed summaries of measurable indicators, independent audits of information, dynamic economic analyses of incentives and a determination of incentives' cost-effectiveness.

Questions and comments from committee members included the following.

- Why are some of the incentives so complex? Mr. Clifford said that some health care incentives have proven to be more complex than initially thought. There are many gray areas in types of medical services, and it is difficult to interpret criteria to qualify for an incentive. Many businesses have also expressed concern about the long amount of time it takes the TRD to approve some credits.

- How regressive is New Mexico's tax burden? Mr. Clifford said that the lowest-income households pay 10 percent of their incomes in taxes, compared to seven percent for middle-income households. State spending, however, is very progressive. Looking at tax burdens on businesses, New Mexico ranks average among states, if severance taxes are excluded from the calculation.

- If New Mexico broadened its tax base to ensure that everyone is taxed, could tax rates be lowered? Mr. Clifford said that policy is theoretically possible, but it would be easier when the state is not facing budget shortfalls. The GRT pyramiding problem is significant; studies indicate that the effective GRT paid is much higher than the statutory rate.

- Pyramiding is a problem, but the legislature continues to narrow the tax base and raise rates. Mr. Clifford said that the recent one-eighth percent increase in the GRT rate raised $50 million in revenues, compared to the $217 million lost from the narrowing of the base from the food deduction. The corporate income tax (CIT) also has a very narrow base, such that most businesses in the state do not pay the CIT.

- How can economists study the economic activity that would have occurred if the tax incentive were not in place? Mr. Clifford said that those studies are very complicated, but that they need to be performed periodically in order to evaluate the complete economic impact of an incentive. He said that even though a business relocation may appear to be beneficial to the state, the costs of the state's provision of government services to those businesses and employees need to be considered.

- The differential between the motor vehicle excise tax rate of three percent and the GRT rate has been discussed by policymakers for years.

- Mr. Clifford was asked to research the types of insurance transactions that are not taxed at all in New Mexico.

Cable Television Update

Susan Bitter Smith, executive director, and Scott Scanland, lobbyist, Arizona-New Mexico Cable Communications Association; Shirley Getz of Cable One; and Chris Dunkeson of Comcast updated the committee on the cable telecommunications industry in the state. Ms. Bitter Smith said that the association represents several smaller cable television providers in addition to Comcast and Cable One. The cable television industry is regulated by the Federal Communications Commission (FCC) and is also regulated and franchised by local communities. Franchise fees are paid to municipalities, and communities are able to design listings according to their own needs. The cable television industry is committed to providing broadband access to the entire state. Comcast has more than 200,000 subscribers and 505 employees in New Mexico. Its total tax liabilities and franchise fees amount to more than $8.6 million. Cable One has 25,000 subscribers and 60 employees in the state. It pays $750,000 in franchise fees, $200,000 in property taxes and $1.4 million in GRT each year.

Questions and comments from committee members included the following.

- Is the cable television industry regulated by the PRC? Ms. Bitter Smith said that the FCC is in charge of regulating the industry.

- To what extent do cable television companies in the state compete with the telephone company Qwest? Ms. Bitter Smith said that although the industries compete on some services, Qwest is a state-regulated utility that has a guaranteed rate of return for some services. Unlike Qwest and other phone companies, the cable television industry is entirely privately capitalized.

- Do cable television rate increases go through an approval process? Mr. Dunkeson said that some municipalities regulate rates, provided that authority is in their franchise agreement.

- Mr. Dunkeson was asked to provide the committee with a list of the amounts Comcast pays in franchise fees, property taxes and GRT.

- Some people feel that the provision of internet access is a function of a public utility and should be regulated by state utility commissions. Ms. Bitter Smith said that she believes the FCC will soon provide nationwide regulations in this arena. The cable television industry does not support state-by-state regulation of the provision of internet services.

The minutes of the October 25-26, 2010 meeting of the committee were adopted without changes.

Tax Incentive Discussion

Ms. Ray led the committee in a discussion about possible legislation for the committee's endorsement. Committee members decided to consider endorsement of legislation at its December meeting. Ms. Ray presented the following three proposed bills for the committee to consider.

- Repealing the Venture Capital Investment Act, which credit has never been used since its enactment in 1993. Staff was instructed to consult with a state venture capital association prior to the committee's endorsement.

- Making uniform the calculation of modified combined tax liability for tax credit purposes. There are currently many statutory tax credit provisions that allow a credit against multiple taxes, but all of these use slightly different definitions of which taxes can be used and of how liabilities are calculated.

- Allowing the TRD to share certain confidential taxpayer information with the legislature, which will allow the legislature to determine the effectiveness of tax incentives. Ms. Ray said that the TRD has commented on the current version of the legislation. The TRD indicated that broad disclosure requirements could be a disincentive for businesses to engage in the targeted activity.

The committee discussed other legislation for consideration at the December meeting, including the sunsetting of all tax incentives; the periodic review of every tax exemption, credit and deduction; the capping of the total amount of some tax credits; the repeal of unused or ineffective tax incentives; the conversion of all exemptions to deductions or credits to ensure that they are reported; and the review of all earmarked revenue sources.

The committee, upon the recommendation of Speaker Lujan, decided that it may need to meet an additional day, on December 16, in addition to the December 15 meeting date.

There being no further business, the committee adjourned at 12:45 p.m.

REVENUE STABILIZATION AND
TAX POLICY COMMITTEE

Section 9

December 2010
Agenda
Minutes

Revised: December 14, 2010

TENTATIVE AGENDA
for the
SEVENTH MEETING IN 2010
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

December 15, 2010
Room 307, State Capitol
December 16, 2010 (if necessary)
Room 309, State Capitol
Santa Fe

Wednesday, December 15

9:30 a.m.	**Call to Order** —Representative Edward C. Sandoval, Chair
9:35 a.m.	**Revenue Forecast** —Dannette Burch, Secretary-Designate of Finance and Administration —Duffy Rodriguez, Secretary-Designate of Taxation and Revenue —Tom Clifford, Chief Economist, Legislative Finance Committee
10:45 a.m.	**Natural Gas Propelled Vehicle Conversion Income Tax Credits** —Speaker of the House Ben Lujan
11:45 a.m.	**Insurance Premium Tax Collection and Administration — Move to Taxation and Revenue Department** —Pam Ray, Staff Attorney, Legislative Council Service (LCS)
12:45 p.m.	**Lunch**
1:45 p.m.	**Endorsements — Review of Proposals** —Pam Ray, Staff Attorney, LCS
4:00 p.m.	**Recess**

Thursday, December 16

9:30 a.m.	**Reconvene (If Necessary)** —Representative Edward C. Sandoval, Chair
9:35 a.m.	**Endorsements (Continued)** —Pam Ray, Staff Attorney, LCS
12:00 noon	**Adjourn**

MINUTES
of the
SEVENTH MEETING IN 2010
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE
December 15, 2010
Room 307, State Capitol
Santa Fe

The seventh meeting of the Revenue Stabilization and Tax Policy Committee (RSTP) for 2010 was called to order by Representative Edward C. Sandoval, chair, on Wednesday, December 15, 2010, at 9:34 a.m. in Room 307 of the State Capitol in Santa Fe.

Present
Rep. Edward C. Sandoval, Chair
Sen. John Arthur Smith, Vice Chair
Sen. Carlos R. Cisneros
Rep. Nathan P. Cote
Rep. Anna M. Crook
Sen. Dianna J. Duran
Rep. Keith J. Gardner
Sen. Timothy Z. Jennings, Senate President
Pro Tempore
Sen. Timothy M. Keller
Sen. Gay G. Kernan
Rep. Ben Lujan, Speaker of the House
Rep. Rodolpho "Rudy" S. Martinez
Sen. Howie C. Morales
Rep. Henry Kiki Saavedra
Rep. Thomas C. Taylor
Rep. Jim R. Trujillo

Absent
Sen. Tim Eichenberg
Sen. William E. Sharer

Designees
Sen. Mark Boitano
Sen. Phil A. Griego
Rep. Luciano "Lucky" Varela (attending as a guest)

Rep. Ray Begaye
Rep. Donald E. Bratton
Rep. Zachary J. Cook
Sen. Kent L. Cravens
Rep. Miguel P. Garcia
Rep. Roberto "Bobby" J. Gonzales
Sen. Clinton D. Harden, Jr.
Rep. Sandra D. Jeff
Sen. Carroll H. Leavell
Rep. Antonio "Moe" Maestas

Sen. Steven P. Neville
Rep. Debbie A. Rodella
Sen. Nancy Rodriguez
Sen. Bernadette M. Sanchez
Sen. John M. Sapien
Rep. James R.J. Strickler
Rep. Don L. Tripp
Sen. Peter Wirth

Other Guest Legislator Attending
Sen. Rod Adair

Staff
Pam Ray, Legislative Council Service (LCS)
Doris Faust, LCS
Ric Gaudet, LCS
Damian Lara, LCS

Minutes Approval

Because the committee will not meet again this year, the minutes for this meeting have not been officially approved by the committee.

Wednesday, December 15

Revenue Forecast

Secretary-Designate of Finance and Administration Dannette Burch, Secretary-Designate of Taxation and Revenue Duffy Rodriguez, Clinton Turner, chief economist, Taxation and Revenue Department (TRD), and Tom Clifford, chief economist, Legislative Finance Committee (LFC), presented to the committee the December consensus revenue estimate and economic outlook for New Mexico. Secretary-Designate Burch began by reporting to the committee that the new consensus revenue estimate has raised revenue projections by $56 million since the October estimate. This represents a 1.1 percent upward revision of the October estimate, which indicates that the bottom of the economic cycle has been realized and New Mexico is experiencing slow economic growth. Changes in the forecast are due largely to expected increases in gross receipts tax (GRT) revenue and federal mineral leasing revenue.

Secretary-Designate Burch said that the final audit for fiscal year 2010 would be issued soon and there would be no changes in revenue projections from the audit. Based on the Department of Finance and Administration's (DFA) final general fund report for fiscal year 2010, the department will transfer $172.6 million from reserve accounts to the general fund to close out the year. Fiscal year transfers to balance the books are estimated to total $39.6 million. The legislature authorized the administration to reduce general fund allotments to agencies if consensus revenue forecasts indicate a deficit will occur. The July 2010 revenue estimates resulted in allotment reductions of $150.9 million, and the October estimates indicated an additional $18.5 million shortfall. However, the December revenue estimates eliminated the need for any further fiscal year 2011 allotment reductions.

Mr. Turner reviewed the economic outlook for the state, which is projected to experience moderate growth in the next year. The GRT base is expected to grow 3.8 percent in the next year. With the inclusion of recent GRT rate increases, GRT revenues are expected to grow by 6.8 percent. Personal income tax (PIT) revenue for fiscal year 2010 is expected to be $957 million, which is more than $250 million lower than fiscal year 2008 levels. PIT revenue is expected to increase to $1.05 billion in fiscal year 2011 and increase slightly each subsequent year. Fiscal year 2008 levels will not be reached again until fiscal year 2015. Corporate income tax (CIT) revenue is expected to increase 76 percent in fiscal year 2011 to $220 million. CIT revenues are expected to increase more than 10 percent each year for the next several fiscal years.

Oil and gas tax revenues are estimated using price and production projections. The price of oil is expected to increase slightly each year. Oil volumes are also expected to increase in fiscal year 2011 but decline one percent per year afterward. Gas prices have remained below $4.00 per 1,000 cubic feet since September and are expected to increase only slightly due to large inventories in the national market. Although the dry gas price has remained low, New Mexico has benefitted from the premiums being paid for liquid gas products. Natural gas volumes in New Mexico have decreased 60 percent since 2008, and long-term predictions indicate that natural gas production will continue to slowly decline.

New Mexico's unemployment rate is currently at 8.8 percent. The Workforce Solutions Department expects the unemployment rate to slowly decrease over the next year, but that it will take several years before job creation eliminates the labor market slack created by the recession.

Mr. Clifford said that New Mexico is experiencing a very uneven economic recovery. Although overall gross domestic product (GDP) has increased, the retail and construction sectors are still in decline. National economic predictions have shown an overall growth rate of 2.5 percent in the next year. If the recently proposed tax incentive package Congress is considering is enacted, growth is expected to be three percent. Mr. Clifford said that New Mexico tax revenue would decline slightly from the tax cuts because the state uses the same income tax calculations that the federal government uses. Assuming a 4.4 percent revenue growth in fiscal year 2012, the deficit for the year, assuming the same level of services, will be $410 million.

Questions and comments from committee members included the following:

- The Tobacco Settlement Permanent Fund (TSPF) should not be considered a reserve for the general fund because money in that fund is not really available to be spent. If the TSPF is not considered a reserve fund, then operating reserves would actually be 2.7 percent and not the reported 4.5 percent.

- Do the projected increases in revenues from the rate increase of the cigarette tax take into account declines in smoking from the tax increase? Mr. Clifford said that the $.75 rate increase was predicated on tribes imposing the same $.75 tax on cigarettes. Tribes still have a $.91 differential with the rest of the state. Sales have not decreased very much since the tax rate increased.

- What would be the effect on CIT revenues from requiring multistate corporations to file combined tax returns? Mr. Clifford said that predicting the revenue impact of combined reporting legislation is difficult. He estimated a 10 percent to 15 percent increase in the CIT base from the change. However, corporations would be able to take other steps to minimize their long-term liabilities. Another idea would be to add back to a company's net income certain specific transactions that are considered to be purely tax avoidance schemes.

- Oil prices may actually rise above $100 per barrel, according to some estimates. Mr. Clifford said that oil prices have gone above $100 per barrel only once in history, during the recent economic bubble. It would not be wise to predict state revenues based on high oil prices.

- Dedicating five percent of the distribution from the Severance Tax Permanent Fund (STPF) for projects in colonias may be necessary, but those communities should also be required to provide some sort of in-kind contribution to the projects.

- The state relies on high cigarette taxes as a revenue source but then does not allow people to smoke in public places.

- State-funded capital outlay projects generate GRT revenue, which should be distributed to the state. Mr. Turner said that statewide, 56 percent of GRT revenues are distributed to the state.

- Infrastructure projects in colonias will allow economic development in those areas. Funding of those projects could be eventually phased out after basic infrastructure needs are met.

- Will capital outlay projects that get funded from a five percent distribution from the STPF on tribal lands generate GRT revenue for the state? Mr. Clifford said that most of those projects will still be part of the GRT base, except for projects that are performed completely by tribal entities. He said that many tribes have cooperative GRT revenue-sharing agreements with the state.

- Funding highway construction projects no longer creates the number of jobs that it used to because new highway construction technology requires fewer employees. Mr. Turner said that job training will be a critical component of the economic recovery. Former construction and manufacturing workers will not be getting jobs in the expanding health care sector without retraining.

- There has been discussion about dedicating funding for highway projects so that highways and bridges stay maintained and highway contractors would be able to keep their employees employed for the long term. Previous highway funding initiatives meant that there would be a large increase in employment, followed by a large decrease when the money ran out.

Natural-Gas-Propelled Vehicle Conversion Tax Credits

Speaker Lujan and Karin Foster, executive director, Independent Petroleum Association of New Mexico, presented a proposed bill to the committee to provide incentives for the purchase or conversion of vehicles that use natural gas instead of gasoline. The bill also encourages retail businesses selling gasoline to expand into dispensing natural gas for vehicle fuel. A PIT and CIT credits are proposed to provide for 70 percent of the cost, after any federal credit is applied, of converting motor vehicles to use natural gas. The PIT and CIT tax credits for expansion of a retail business to sell natural gas are for 50 percent of the cost. Finally, vehicles that are purchased new with natural gas as their power source will be exempt from the motor vehicle excise tax. The tax credits and exemption will end after five years.

Questions and comments from committee members included the following:

- How does a unit of gasoline compare to a unit of natural gas? Ms. Foster said that a gallon of compressed natural gas (CNG) has about the same performance as a gallon of gasoline. Currently, natural gas is selling at $1.00 less per gallon than gasoline. She said that the natural gas industry is willing to pay the current gasoline tax rate on sales of natural gas in order to ensure the solvency of the State Road Fund.

- What is the cost of conversion to natural gas? Ms. Foster said that a motor vehicle conversion costs about $12,000. It costs about $1.5 million to convert a gas station into a "fast-fill" natural gas station. Most fleet vehicles are currently refilled at less costly "slow-fill" facilities, but the refilling process takes several hours. The CNG industry needs retail infrastructure throughout the state in order for CNG-powered vehicles to become viable.

- Why is an incentive needed for vehicle conversions since people will be paying much less for fuel than for gasoline? Speaker Lujan said that this new technology needs to be supported at the beginning, in order to get people interested in using CNG in their vehicles.

Premium Tax Collection and Administration — Move to TRD

Ms. Ray presented legislation for the committee's consideration that would transfer the collection of the premium tax from the Public Regulation Commission (PRC) to the TRD. Ms. Ray said that the committee had previously expressed concern that the administration of the premium tax and related health insurance premium surtax was not being collected efficiently. The TRD may be a better entity to collect the taxes.

Questions and comments from committee members included the following:

- Is the TRD in favor of the legislation? Secretary-Designate Rodriguez said that the TRD has not yet considered the bill.

- Does the PRC collect any other taxes? Ms. Ray said that the Insurance Division of the PRC does not collect any other taxes. It does, however, collect many different fees. David Lucero, analyst, LFC, said that the annual cost for administration of the premium tax is $420,000. The PRC has seven full-time employees that administer the system. The premium tax and surtax generate $200 million annually.

● How is the administration of the tax paid for? Mr. Lucero said that the PRC collects an administrative fee before revenue is distributed. Ms. Ray said that the current legislation does not provide for transfer of staff from the PRC to the TRD.

● The bill needs to be amended to include the transfer of surplus lines insurance premium tax collections.

The minutes of the November 29-30 meeting of the committee were adopted without changes.

Endorsements — Review of Proposals

The committee considered the endorsement of 14 proposed bills.

1) Repeal Venture Capital Investment Act. Ms. Ray said that this credit has never been used due to its complexity. The enactment of the angel investment credit has eliminated the need for the credit.

The committee endorsed the legislation unanimously.

2) Define "Modified Combined Tax Liability". Jim O'Neill, consultant and former TRD employee, said that the proposed bill fixes two technical issues in statute. When credits are allowed against various taxes, the question has arisen whether the calculation of distributions to local governments should reflect the credits taken. The TRD determined administratively 30 years ago that local governments should receive the full amount of the distribution without taking into account the credits. The proposed bill merely puts into statute what has been in practice for three decades. The bill also provides a uniform definition of "modified combined tax liability" for the various credits so that the TRD can administer the credits more efficiently. Taxpayers will not see any change from enactment of the bill, he said.

The committee endorsed the legislation, with Speaker Lujan voting against endorsement.

3) Confidentiality Exceptions for Tax Incentive Reporting. Ms. Ray said that this bill allows the TRD to disclose information about tax credits that otherwise would not be allowed. When a tax credit or incentive is claimed by only a few taxpayers, the TRD is not allowed to disclose any information about the cost of the credit because doing so would provide information about those individual taxpayers. The proposed bill would allow the TRD to disclose information it deems essential to assess the effectiveness of a tax incentive.

Committee members expressed concern that information about recipients of low-income tax benefits would be revealed by the TRD. Some members felt that the bill needs to be revised before it could be endorsed.

The committee voted to not endorse the bill, with Representatives Cote, Martinez and Saavedra and Senators Smith, Cisneros, Keller and Morales voting to endorse and

Representatives Sandoval, Crook, Lujan, Taylor and Trujillo and Senators Griego, Kernan and Boitano voting not to endorse.

4) Itemized Reporting of Combined Reporting System (CRS) Deductions. Senator Keller said that in general, all deductions and exemptions from CRS taxes will be reported if the legislation is enacted. Most deductions currently are reported in the aggregate, which makes it difficult for the TRD to calculate the cost of each deduction. The bill will also require gross receipts to be reported for exempt transactions.

Committee members asked about the kinds of nonprofit organizations that will now be required to report their gross receipts. Ms. Ray said that most nonprofit entities that currently are exempt from the GRT will be required to report their gross receipts.

The committee adopted the legislation, as amended to delete new language that asserted the presumption that all nonprofit entities are subject to the GRT. Senator Kernan voted against endorsement.

5) Film Production Tax Credit Changes. Senator Keller said that the bill provides tracking requirements for film production companies claiming the credit; requires the posting of contact information for film production companies until all financial obligations in the state have been satisfied; requires an application for the credit to be made within one year of the company making final expenditures on a film; requires income tax to be withheld at the maximum statutory rate; requires a physical presence in New Mexico for expenditures to qualify for the credit; and requires the Economic Development Department (EDD) to provide an annual report on the credit's effectiveness.

Questions and comments from committee members included the following:

- The definition of "physical presence" is subject to interpretation by the New Mexico Film Division of the EDD. Lisa Strout, director, New Mexico Film Division, said that the place of business must be commensurate with the type of services being provided. Division staff will need to verify that a business qualifies as having a physical presence. Currently, some companies qualifying for the credit have a physical presence on paper only. This will mean additional responsibilities for the division, but the credit is intended to support New Mexico businesses.

- Will the new reporting requirements discourage the film industry from making films in the state? Ms. Strout said that the film industry is willing to comply with the additional reporting requirements.

- How will the film auditor hired by the State Investment Council (SIC) affect revenue to the state? Ms. Strout said that film audits are a standard procedure in the film industry. The state should be receiving revenue soon from investments it made through the SIC from several film productions.

The committee endorsed the legislation unanimously, as amended to correct a typographical error.

6) Tax Expenditure Budgeting. Senator Keller said that this bill is the same as a bill that was passed by the legislature in 2007 but was vetoed. It requires the TRD to compile a tax expenditure budget that lists the costs and benefits of all tax expenditures.

The committee endorsed the legislation unanimously.

7) Electric Plug-In Vehicle Tax Credit. Ms. Ray said that the bill exempts from the motor vehicle excise tax the purchase of new electric plug-in vehicles.

Committee members expressed concern that the exemption could apply to electric golf carts as well as the new cars being brought to the market.

The committee endorsed the legislation unanimously, as amended if necessary to clarify the golf cart issue.

8) Jet Fuel Deduction Extension. The bill would extend until 2017 the current 55 percent deduction from gross receipts and from computing the compensating tax of the sale of jet fuel.

The committee endorsed the legislation unanimously.

9) PIT Credit for Certain Out-of-State Employees. Ms. Ray said that the bill would provide a PIT credit of up to $1,000 for certain out-of-state employees of New Mexico logistics and distribution companies located in the border region of Santa Teresa.

The committee voted unanimously to not endorse the legislation.

10) Federal Low-Income Housing Credit Use in Property Valuation. Ms. Faust said that the bill is intended to end the divergent treatment by county assessors of property that has taken advantage of federal low-income housing credits to provide affordable housing. Some county assessors have added the value of the tax credit to the property assessment, which makes the development of these housing units no longer cost-effective.

Committee members expressed opposition to the bill and discussed that the real problem is that county assessors are not following the law in assessing properties. The bill is not needed because current law already mandates that county assessors take into consideration the decrease in value that would be realized by the owner in a sale of the property.

The committee voted unanimously to not endorse the legislation.

11) Above-Ground Storage Tank Installation Credit. Ms. Faust informed the committee that supporters of the legislation have withdrawn the bill from the committee's consideration. She said that the parties are pursuing a different resolution to the problem of complying with the state requirement of installing double-walled storage tanks by July 2011.

12) Natural-Gas-Propelled Vehicle Tax Credits. This bill had been presented to the committee earlier in the day. Speaker Lujan said that the fiscal impact from the legislation was estimated in the 2010 legislative session to be $3 million.

A committee member said that the credit for the installation of equipment to deliver CNG at retail stations is needed, but the vehicle conversion credit is probably not needed.

The committee endorsed the legislation unanimously.

13) Premium Tax Collection Change to TRD. This bill had been presented to the committee earlier in the day. Ms. Ray said that, after discussing the surplus lines premium tax with PRC staff, she believes that administration of that tax should not be switched to the TRD. PRC staff need to verify on a regular basis the tax, which is paid by out-of-state insurance companies.

Superintendent of Insurance John Franchini said that the premium tax and surtax generate $215 million annually for the state. The Insurance Division has four people who administer the tax. He said that the division is very efficient at collecting the tax and performing audits. Every time an insurance policy is written, the amount of tax due is reported to the PRC. PRC staff also audit every insurance company's financial statements to ensure compliance. The surplus lines premium tax is very complicated, and that insurance structure is currently being modified by the federal government. The administration of the premium tax does not need to be transferred to the TRD.

The committee voted unanimously to not endorse the legislation.

14) Provide for Review of Certain Tax Credits. Ms. Ray said that the bill provides for a periodic review by the committee of 28 tax credits. She said that the bill provides for review of the more commonly used economic development credits. She asked for input from the committee whether the review should be every four years or six years.

Questions and comments from committee members included the following:

- A four-year review period may send the message to businesses that the credit will be repealed, which may inhibit businesses to make investments in the state.

- Credits should have a specific date on which they expire, which still allows for a periodic review.

The committee endorsed the legislation unanimously.

There being no further business, the committee adjourned for the year at 3:04 p.m.

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REVENUE STABILIZATION AND
TAX POLICY COMMITTEE

Section 10

2010

Legislative Proposal Chart
Endorsed Legislative Proposals

REVENUE STABILIZATION AND TAX POLICY COMMITTEE
LEGISLATIVE ENDORSEMENTS FOR 2011 LEGISLATIVE SESSION
DECEMBER 15-16, 2010

Draft #	**Title**	**Agency**	202#	Endorsed Sponsor	Summary
1	**Repeal the Venture Capital Investment Act**	**RSTP**	.182794.1	Sen. Smith Endorsed	Repeals unused (since 1993) Venture Capital Investment Act, which was replaced generally by the angel investment tax credit.
2	**Defining "Modified Combined Tax Liability"**	**RSTP**	.182793.2	Rep. Crook Endorsed	Makes definitions used in tax credits taken against major CRS taxes uniform.
3	**Tax Information Confidentiality Exceptions for Incentive Reporting and Analysis**	**RSTP**	.183203.3	Not Endorsed	Provides for exception to allow taxpayer information to be reported to the legislature.

4	**Requiring Taxation and Revenue Department (TRD) to Revise Tax Reporting Forms for Itemization of Exemptions and Deductions**	**Sen. Keller**	.182782.2	Sen. Keller Endorsed	For Gross Receipts and Compensating Tax Act only; requires persons taking GRT deductions to itemize them; identifies the exemptions that require filing.
5	**Film Production Tax Credit Changes**	**Sen. Keller**	.182789.3	Sen. Keller Endorsed	Tightens up the reporting requirements for the film production tax credit; also requires physical presence in NM of vendors claimed as NM vendors.
6	**Tax Expenditure Budgeting**	**Sen. Keller**	.183341.1	Sen. Keller Endorsed	Provides for creation of tax expenditure budgets.

7	**Electric Plug-In Vehicle Tax Credit**	**Rep. Trujillo**	.183346.1	Rep. Trujillo Endorsed	Provides for a credit for electric plug-in vehicles purchased from motor vehicle excise tax and a deduction from GRT equal to the gross receipts from the sale of the car; there is a compensating tax credit also.
8	**Jet Fuel Gross Receipts Tax and Compensating Tax Deduction Extension**	**Rep. Sandoval**	.182936.1	Sen. Griego Endorsed	Extends the period for a tax credit of 55% of jet fuel sold for use in turbo-prop or jet engines until June 30, 2017; was to be reduced to 40% in 2012.

9	**PIT Credit for Out-of-State Residence Property Tax Paid**	**Sen. Nava**	.182765.2	Not Endorsed	For employees of manufacturing, distribution and logistics businesses within 20 miles of the international border.
10	**Federal Low-Income Housing Credit (FLIHC) Use in Valuation of Property**	**Rep. Gonzales**	.182525.1	Not Endorsed	Excludes the value of FLIHC from inclusion by an assessor in the value of property where FLIHC is claimed.
11	**Above-Ground Storage Tanks**	**Sen. Sapien**	.182742.1	Not Endorsed	Allows taxpayer to claim credit for 50% of value of replacing an above-ground fuel tank against PIT or CIT.

12	**Natural Gas Propelled Vehicles Income Tax Credit**	**Speaker Lujan**	.183540.1	Speaker Lujan Endorsed	HB 282 (2010 reg.) provides GRT, PIT or CIT tax credits for conversion of vehicles or installation of NG dispensers; also MV excise tax deduction.
13	**Premium Tax/Health Premium Surtax — Relocate Collection and Administration to TRD**	**RSTP Suggestion for Restructuring**	.183555.2	Not Endorsed	Moves the collection and administration of the premium tax and health premium surtax to the TRD.
14	**Provide for Review of Certain Tax Credits**	**RSTP**	.183558.1	Rep. Sandoval Endorsed	Requires the RSTP to review 28 tax credits* every six years, beginning in 2014.

* Cultural property preservation credit — PIT and CIT (Sections 7-2-18.2 and 7-2A-8.6 NMSA 1978)

REVENUE STABILIZATION AND TAX POLICY COMMITTEE
LEGISLATIVE ENDORSEMENTS FOR 2011 LEGISLATIVE SESSION
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Restricted land use conveyances — PIT or CIT (Sections 7-2-18.10 and 7-2A-8.9 NMSA 1978)
Job mentorship programs tax credit — PIT or CIT (Sections 7-2-18.11 and 7-2A-17.1 NMSA 1978)
Solar market development tax credit — PIT (Section 7-2-18.14 NMSA 1978)
Angel investment credit — PIT (Section 7-2-18.17 NMSA 1978)
Renewable energy production tax credit — PIT and CIT (Sections 7-2-18.18 and 7-2A-19 NMSA 1978)
Sustainable building tax credit — PIT and CIT (Sections 7-2-18.19 and 7-2A-21 NMSA 1978)
Blended biodiesel fuel credits — PIT and CIT (Sections 7-2-18.21 and 7-2A-23 NMSA 1978)
Rural health care practitioners credit — PIT (Section 7-2-18.22 NMSA 1978)
Geothermal ground-coupled heat pump tax credits — PIT and CIT (Sections 7-2-18.24 and 7-2A-24 NMSA 1978)

Corporate child care credit — CIT (Section 7-2A-14 NMSA 1978)
Rural job tax credits — PIT or CIT (Section 7-2E-1.1 NMSA 1978)
Film production tax credit — PIT and CIT (Section 7-2F-1 NMSA 1978)
Biodiesel blending facility — GRT and Comp (Section 7-9-79.2 NMSA 1978)
Hospital GRT credit — GRT (Section 7-9-96.1 NMSA 1978)
Unpaid doctors' expenses in hospital — GRT (Section 7-9-96.2 NMSA 1978)
Investment tax credit — CRS (Section 7-9A-2.1 NMSA 1978)
Lab partnership with small business — GRT (Section 7-9E-11 NMSA 1978)
Technology jobs tax credit — CRS (Section 7-9F-12 NMSA 1978)
High wage jobs tax credit — CRS (Section 7-9G-1 NMSA 1978)
R&D small business tax credit — CRS (Section 7-9H-6 NMSA 1978)