

**NOTE:** As provided in LFC policy, this report is intended only for use by the standing finance committees of the legislature. The Legislative Finance Committee does not assume responsibility for the accuracy of the information in this report when used for other purposes.

The most recent FIR version (in HTML & Adobe PDF formats) is available on the Legislative Website. The Adobe PDF version includes all attachments, whereas the HTML version does not. Previously issued FIRs and attachments may be obtained from the LFC in Suite 101 of the State Capitol Building North.

## FISCAL IMPACT REPORT

SPONSOR: Nunez DATE TYPED: 3/18/03 HB 252/aHTRC

SHORT TITLE: Agricultural Water Tax Credits SB \_\_\_\_\_

ANALYST: Neel

### REVENUE

Estimated Revenue		Subsequent Years Impact	Recurring or Non-Rec	Fund Affected
FY03	FY04			
	(\$20.0)	(\$100.0)	Recurring	General Fund

(Parenthesis ( ) Indicate Revenue Decreases)

Relates to SB 128, Unused Water Forfeiture Exemption

### SOURCES OF INFORMATION

LFC files

#### Responses Received From:

Department of Agriculture  
Office of State Engineer  
Taxation and Revenue Department (TRD)

### SUMMARY

#### Synopsis of HTRC Amendment

The House Taxation and Revenue Committee amended HB 252 to reduce the maximum allowable credit to \$1.0 from \$50.0 for eligible improvements an individual can claim against their income tax liability. Additionally, in promulgating rules in determining whether improvements may qualify for the credit the Soil and Water Conservation Commission is to receive information from the State Engineer.

#### Synopsis of Original Bill

House Bill 252 provides a personal and corporate income tax credit for agricultural water

conservation expenses. It provides for a credit against income tax liability equal to 75 percent of incurred expenses, not to exceed a maximum annual credit of \$50,000, for eligible improvements in irrigation systems or water management methods. A credit may be claimed for the taxable year in which expenses are incurred if the taxpayer in that year: owned or leased a water right appurtenant to the land on which an eligible improvement was made; complies with a water conservation plan approved by the local soil and water conservation district in which the improvement is located; and the improvement is primarily designed to conserve water on land in New Mexico that is owned or leased by the taxpayer and used by the taxpayer or the taxpayer's lessee to produce agricultural products, harvest or grow trees, or sustain livestock.

### Significant Issues

According to the State Engineer, there is little incentive at the present time for irrigators to make improvements to their irrigation systems to conserve water. A tax credit will provide an incentive for making improvements in irrigation efficiency.

As proposed in this bill, a preferable way to encourage water conservation is to provide tax incentives to those who invest in drip irrigation and other water conservation techniques. If irrigators attempt to increase the number of acres irrigated using conserved water, or attempt to lease this water to other farmers, this will increase the total consumptive use of water which could reduce return flows and surface water supplies that are available to downstream irrigators.

The rules promulgated by the soil and water conservation commission which establish the guidelines for determining which improvements are eligible for tax credit (Section 1.F of the bill) should be written in such a way as to place certification of eligibility (methods, standards) in the hands of either the soil and water conservation commission or the New Mexico Department of Agriculture.

There should be language in the bill assuring that persons or entities cannot claim a tax credit as a person and as corporation but only as one or the other.

### **FISCAL IMPLICATIONS**

The fiscal impact has been revised down proportionally from the original tax credit. The amended bill changes the maximum allowable credit from \$50.0 to \$1.0 or 98 percent. The associated fiscal impact has been amended accordingly to \$20.0 in FY04 and \$100.0 in subsequent years.

TRD notes the following assumptions in determining the fiscal impact:

According to the Water Use and Conservation Bureau of the Office of the State Engineer, there are over 1 million acres of irrigated cropland in New Mexico. The USDA Economic Research Service reports that farms in New Mexico spend about \$70 million per year on repair and maintenance of capital items. The USDA reports that net farm income was approximately \$500 million in 2000.

These data suggest that irrigation expenditures are a major category of spending for farm operations in New Mexico. The revenue estimate assumes these expenditures comprise roughly one-tenth of the total capital and maintenance budget, or about \$7 million per year. The annual value

of the credit would then be 75% of this amount, or about \$5 million per year. This estimate is only an approximation of the potential impacts of the proposal because the Department does not have detailed information on irrigation expenses.

The FY 2004 estimate reflects adjustments to tax payments for the first six months of tax year 2004

### **TECHNICAL ISSUES**

TRD notes that HB 252 would require the development of mechanisms to verify that the tax basis of the equipment is decreased by the amount of the credit. The mechanisms would be manual by nature. Modifications will be required in forms and instructions for both personal income tax and corporate income tax, systems and training for department personnel. Therefore, the department would require an additional FTE to carry out the associated tasks.

The measure would probably not allow owners of S-corporations to share the credit. Owners of S-corporations are co-owners of the corporation not co-owners of the land. If the intent is for owners of S-corporation to share the credit, the term "pass-through entity" should be employed in statute. An example of this type of language would be similar to: "If a pass-through entity (S-corporation partnership or limited liability company) owns the land on which an eligible improvement in irrigation systems or water management method is made, the owners of the entity may claim a pro rata share of the credit allowed....".

If HB 252 and SB 128, *Unused Water Forfeiture Exemption* were enacted into law the potential sale of water rights under SB 128 may help mitigate the general fund revenue loss included in HB 252.

SN/njw:yr