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

SPONSOR: Aragon DATE TYPED: 10/29/03 HB

SHORT TITLE: Omnibus Tax and Highway Bill SB 5

ANALYST: Taylor, Neel, Valenzuela

APPROPRIATION

Appropriation Contained		Estimated Additional Impact		Recurring or Non-Rec	Fund Affected
FY04	FY05	FY04	FY05		
	700.0			Recurring	Weight Distance Tax Identification Permit Administrative Fund

(Parenthesis ( ) Indicate Expenditure Decreases)

REVENUE

Estimated Revenue		Subsequent Years Impact	Recurring or Non-Rec	Fund Affected
FY04	FY05			
(400.0)	$55,900.0	$23,300.0	Rec/Non-Rec	General Fund
6,600.0	73,800.0	75,800.0	Recurring	State Road Fund
	8,000.0	8,000.0	Recurring	Other State Funds
	(2,200.0)	11,600.0	Recurring	Local Gov't Funds

(Parenthesis ( ) Indicate Revenue Decreases)

SOURCES OF INFORMATION

NM Taxation and Revenue Department (TRD)
NM Department of Transportation (DOT)
NM Finance Authority (NMFA)

SUMMARY

Senate Bill 5 proposes numerous changes to the New Mexico tax system. The proposed changes have significant fiscal implications for the state road fund. This reflects the interest in providing additional resources to that fund, reflecting the State Department of Transportation, the Governor's Office and the Blue Ribbon Tax Commission reports that road fund revenue sources are insufficient to meet the state highway financing needs.

The overall fiscal impact on the road fund is an increase of nearly $74 million in FY05, the first full year of changes. Although there are some significant changes in particular taxes affecting the state general fund and local government funds, the overall fiscal impact on these funds is limited. Presumably, this reflects the intent of the sponsors to propose a change in the system that approaches revenue neutrality for these entities. The relatively small, positive effect on the general fund--nearly $56 million in FY05--includes both recurring and non-recurring components. While the changes in FY05 are technically recurring, they are partially offset by recurring reductions in FY06. Most of these simply reflect differences in the effective dates for proposed changes. The recurring revenue implication for the general fund is approximately $23 million.

Finally, the numbers reported in this analysis should be considered preliminary. All impacts are reported on a full year basis on the assumption that the Department of Finance and Administration will have implemented accounting changes affecting the timing of revenue recognition (GASB 34). Also, reports on some aspects of the bill still had not been provided by state agencies, and LFC staff was unable to review the reasoning behind this set of estimates. The report will thus be updated as material information becomes available.

SYNOPSIS OF BILL

Streamlined Sales Tax. The bill titles Sections 1 through 9 as the "Sales and Use Tax Administration Act". The bill finds that simplified sales and use taxes will serve to preserve and strengthen these taxes as a revenue source for state and local government and will reduce the administrative burden on sellers. The bill allows the state, represented by the Taxation and Revenue Department (TRD) Secretary, to participate with other states that have sales taxes in negotiating the streamline sales tax initiative. Implementation of the agreement requires adoption by the state legislature. Effective date: Upon signature with two-thirds vote; if not, February 2004.

Local Option Compensating Tax. Section 10 defines the "local option compensating tax", thereby allowing municipalities and counties to impose the compensating tax. Effective date: July 1 2005.

Distribution to State Road Fund. Section 11 strikes the distribution of the weight distance tax administrative fee to the road fund. These fees are later directed to TRD, a step necessary for the administration of the weight distance identification card (a.k.a. cab card). Effective date: July 1, 2004.

Local Option Compensating Tax. Sections 12 through 15 provide for the transfer of local option compensating tax revenues which would be collected by TRD to municipalities and counties. Section 15 determines the jurisdiction where use of property subject to the local option compensating tax occurs. Effective Date: July 1, 2005.

Special Fuel Excise Tax Distribution. Section 16 reduces the percentage of special fuel excise taxes distributed to the local government road fund from 11.11 percent to 8.7 percent. Distributions are changed to direct additional special fuel tax revenues to the state road fund; local distributions are held harmless. Effective Date: July 1, 2004.

Distribution of Liquor Excise Tax. Section 17 reduces the percentage of liquor excise tax revenues to the DWI grant fund from 34.57 percent to 12.3 percent of net receipts. This section also provides for a new 7.6 percent of net receipts distribution to municipalities. Distribution to specific municipalities is determined by two equally weighted factors: share of the state population living in the municipality and the share of state taxable gross receipts attributable to the municipality. Finally, it provides for a new distribution to counties equal to 1.4 percent of net receipts. Distribution to specific counties is determined by the same two-factor formula used for municipal distributions. Effective Date: March 1, 2004.

Tax Administration Issues. Sections 18 through 23 address tax administration matters. Section 18 increases the minimum tax liability threshold after which TRD must assess the taxpayer from ten dollars ($10.00) to twenty-five dollars ($25.00). Section 19 allows taxpayers to elect the "Rules of Civil Procedures for the District Courts" in TRD administrative hearings. Section 20 provides taxpayers with the right to designate certain refund claims as a protective claim. A protective claim is a claim for refund filed by someone based upon the arguments advanced by another person in a previously filed claim that has not been resolved. TRD would not take action on the protective claim until the previously filed claim is resolved. Section 21 and 22 change the interest rate charged and paid by TRD on tax deficiencies and overpayments. The current 15 percent rate would be changed to 10 percent on July 1, 2004. Starting January 2006, the rate would be set equal to the IRS underpayment rate—a floating rate that reflects market interest rates. Section 23 increases the minimum penalty for failing to pay or file a tax return by the date due from five dollars ($5.00) to twenty five dollars ($25.00). Effective Date: July 1, 2004.

Tax Exemption on Income of Persons 65 and Older. Section 24 extends the exemption of retirement income so that all persons aged 65 and older would be able to exempt at least $2,500 of income. Currently, the exemption starts at $8,000, gradually decreases at higher income levels, and ends completely at incomes over $51,000 for married persons and $28,500 for single persons. Applicable after January 1, 2004.

Income Tax Filing Categories Reduced. Sections 25 through 28 eliminate the separate personal income tax tables for heads of household and roll the head of household category into the tax tables covering surviving spouses and married persons filing joint returns. The separate tables for head of households imposed higher taxes on that group compared with the married individuals table. Applicable after January 1, 2004.

Low Income Rebates Renamed; Rebate Amounts Increased. Section 29 changes the name of the "Low Income Comprehensive Rebate" to the "Family and Individual Rebate", expands the table to increase the number of exemptions from 6 to 7, broadens the income groupings, lengthens the table so that larger families with incomes between $22,000 and $39,000 receive rebates (as income increases, family size must also increase to be eligible) and increases the rebate amounts. The definition of modified gross income is amended to include the value of food stamp benefits. Applicable after January 1, 2004.

<u>Additional Exemption Amounts</u>. Section 30 increases the value of the personal exemption amount for low and moderate income taxpayers up to a maximum of $3,000 per exemption. The value of the exemption is reduced as income increases up to a maximum amount at which point it goes to zero. The rate of the phased reductions is adjusted for the number of exemptions. Single individuals with adjusted gross income less than $8,000 receive the full $3,000 exemption; the value of exemption is gradually reduced for greater incomes, completely phasing out at $28,000. Married individuals filing joint returns with adjusted gross income less than $18,000 receive the full $3,000 exemption; the value of the exemption is gradually reduced at greater incomes, ending at $48,000. Heads of households with adjusted gross income less than $15,000 receive the full $15,000 exemption; it is gradually reduced at greater incomes and fully phased-out at $40,000. Applicable after January 1, 2004.

<u>Business Services Tax Credit</u>. Section 31 provides a new business services tax credit which may be claimed against the state gross receipts tax, state compensating tax and withholding tax liabilities. The credit is equal to 0.625 percent of the value of qualified business service expenditures, which excludes entertainment, janitorial, repair and maintenance and any other services for which a taxpayer receives another credit. The credit may be claimed within three years of when the expenditure was made. Effective date: July 1, 2005.

<u>High Wage Jobs Tax Credit</u>. Section 32 provides “high wage jobs tax credit” equal to 10 percent of wages and benefits paid to an eligible employee in a new high-wage job up to a maximum of $12,000. To qualify, a job must pay more than $40,000 per year in municipalities with a population greater than 40,000, and $28,000 per year in a municipality with a population below 40,000. Also, to qualify a business must be growing, with employment greater on the last qualifying day of the credit than the day when the new positions were created. The credit may be claimed for the year in which the job is created and for three years thereafter. It can be taken against the taxpayer’s modified combined tax liability (gross receipts tax, compensating tax and others), personal income tax liability or corporate income tax liability. The credit is refundable. Effective date: July 1, 2004.

<u>Research and Development Small Businesses Gross Receipts Deduction</u>. Section 33 and 34 enact a new section of statute to provide a GRT/compensating “tax holiday” for small, high tech research businesses. Qualifying businesses are small firms (no more than 25 employees with revenue of $10 million or less in the prior fiscal year) that have made qualified research expenditures in the last 12 months. Qualified research expenditures exclude expenditures funded with grants, expenditures on property associated with Industrial Revenue Bonds, or property received as part of the Capital Equipment Tax Credit Act, the Investment Credit Act or the Technology Jobs Tax Credit Act. Effective date: July 1, 2004.

<u>Gross Receipts Deduction for Certain Receipts From Services Provided by Licensed Health Care Practitioners</u>. Section 35 provides a gross receipts tax deduction for receipts of licensed health practitioners from payments by a managed care provider for Medicare Part C services or commercial contract services. Commercial contract services are services provided through a contract with a managed care organization other than those provided to Medicare and Medicaid patients. Licensed health care practitioners include physicians, physician assistants, osteopathic physicians, chiropractic physicians, doctors of oriental medicine, dentists, dental hygienists, podiatrists, psychologists, registered nurses, licensed practical nurses, midwives, physical therapists, optometrists, occupational therapists, respiratory care practitioners and speech pathologists. Effective date: January 1, 2005.

Gross Receipts Exemption for Certain Athletics Contests, Sporting Events and Concerts. Section 36 exempts receipts from ticket sales and admission fees to boxing, wrestling, auto racing, one-time sporting events and live concerts held at a venue capable of holding at least 2,500 persons. Effective date: July 1, 2004.

Governmental Gross Receipts. Section 37 expands the definition of governmental gross receipts to include the rental of parking or docking of vehicles, aircraft and boats. Effective date: July 1, 2004.

Compensating Tax on Services. Sections 38 through 41 impose the state and local compensating taxes on services from out of state businesses that have no nexus to the state and which would have been subject to the gross receipts tax had it occurred within the state. A compensating tax municipal credit of one half or one quarter of one percent is also provided, depending on the municipal compensating tax rate. Effective date for section 38: July 1, 2004. Effective date for sections 39-41 July 1, 2005.

Gross Receipts and Compensating Taxes on Motor Vehicles. Sections 42 and 43 exempt new alternative fuel cars from the gross receipts and compensating tax. This section relates to the motor vehicle excise tax exemption provided for these vehicles. Absent this exemption, cars provided the motor vehicle excise tax exemption would fall under the gross receipts and compensating tax provisions. Effective date: July 1, 2004.

Nontaxable Transaction Certificates (NTTCs). Section 44 changes the law associated with NTTC's. It eliminates the requirement that taxpayers be in possession of an NTTC within 60 days from the date required to allow for a deduction. It also provides use of other evidence in certain circumstances, including bankruptcy, death or an entity no longer existing as a business. Effective date: July 1, 2004.

Cigarette Stamps. Section 45 eliminates cigarette tax discounts for small volumes. All cigarette tax stamps would be sold at face value. Effective date: March 1, 2004.

Motor Vehicle Excise Tax Rate. Section 46 increases the motor vehicle excise tax rate from three percent to four percent. It establishes a minimum tax of twenty dollars ($20). Effective date: March 1, 2004.

Motor Vehicle Tax Exemption. Section 47 provides a one-time motor vehicle excise tax exemption for the purchase of clean, fuel efficient vehicles. Qualifying vehicles are defined as vehicles manufactured to run exclusively on alternative fuels with a U.S. environmental protection agency a fuel economy rating of at least 22.5 miles per gallon. Effective date: July 1, 2004.

Leased Vehicle Surcharge Rate. Section 48 increases the surcharge on short term leased vehicles from two dollars ($2) per day to four dollars ($4) per day. Effective date: March 1, 2004.

Weight Distance Tax Identification Permits Defined. Section 49 defines a new "weight distance tax identification permit" that is issued by TRD and identifies a vehicle as subject to the weight distance tax. Effective date: July 1, 2004.

Weight Distance Tax Rates. Section 50 increases weight distance tax rates for vehicles other than buses. Rates, which are established on a mills per mile basis for different gross vehicle weight ranges (a mill is one thousandth of one dollar), are increased by 42 percent. Effective date: July 1, 2004.

Bus Tax Rates. Section 51 increases the weight distance tax rates for buses. Rates, which are established on a mills per mile basis for different gross vehicle weights, are increased by 42 percent. Effective date: July 1, 2004.

Weight Distance Tax Identification Permits. Sections 52 through 54 deal with weight distance tax permit issues. Section 52 requires vehicles subject to the weight distance tax to display and produce on demand a weight distance tax identification permit upon passing a port of entry. Section 53 establishes an administrative fee for the weight distance tax identification permit. Section 54 establishes a non-reverting Weight Distance Tax Identification Permit Administration Fund for depositing associated revenues. Money in the fund is earmarked to TRD to pay for the cost of issuing and administering the permits. Effective date: July 1, 2004.

Special Fuels Tax Rate. Section 55 increases the special fuels tax from $0.18 per gallon to $0.23 per gallon. Effective date: July 1, 2004.

Liquor Excise Tax Rates. Section 56 increases liquor excise tax rates. The rate on spirituous liquors is increased from $1.60 per liter to $3.86—a 140 percent increase. The rate on beer is increased from $0.41 per liter to $1.48—a 260 percent increase. The rate on wine (excluding fortified wine) is increased from $0.45 per liter to $1.13—a 150 percent increase. Effective date: March 1, 2004.

Supplemental Local Government Compensating Taxes. Sections 57 through 70 deal with local government supplemental compensating taxes. Section 57 authorizes municipalities to impose a supplemental compensating tax. The compensating tax rate would be equal to the gross receipts tax rate. Section 58 requires supplemental municipal compensating taxes to conform to the state compensating provisions. Section 59 requires TRD to collect and distribute the local option compensating tax revenues (adjusted for credits and refunds) within the month in which they are collected. Section 60 provides TRD with responsibility for administering and enforcing the collection and distribution of the supplemental compensating taxes. Section 61 establishes that the tax shall be used to pay current bond obligations, new bond issues or may be transferred to any other municipal fund once bonding obligations are met. Section 62 requires that changes to the local option gross receipts tax be matched by changes to the compensating tax. It also automatically implements the local option compensating tax in municipalities that have imposed local option gross receipts taxes. Section 63 governs how TRD is to collect and transfer the municipal local option compensating tax. Section 64 requires entities imposing a local hospital gross receipts tax also impose the local hospital compensating tax. Section 65 governs TRD's collection and transfer of the local hospital compensating tax. Section 66 requires counties to establish a compensating tax that parallels their gross receipts tax. Section 67 governs how TRD and collects and transfers the county compensating tax. Section 68 requires counties with correctional facility gross receipts taxes to also impose a parallel compensating tax. It establishes that the tax will be governed and used in the same manner as the corresponding gross receipts tax. Section 69 governs how TRD is to collect and transfer the county correctional compensating tax. Section 70 provides counties with the authority to pledge and bond correctional compensating tax revenues as they do corresponding gross receipts tax revenues. Effective date: July 1, 2005.

<u>Severance Tax Rate on Oil Production</u>. Section 71 increases the oil and gas emergency school tax rate on oil and carbon dioxide from 3.15 percent to 4 percent. The lower rates provided on oil and other liquid carbons removed from natural gas at stripper wells in times of low oil prices are increased. These rates change from 1.58 percent to 2 percent when the value of the oil is less than $15 per barrel; and from 2.36 percent to 3 percent if the value of the oil is greater than $15 but less than $18. Effective date: March 1, 2004.

<u>Tax Administration—Request for Regulations</u>. Section 72 allows taxpayers or other interested parties to request TRD regulations. Effective date: July 1, 2004.

<u>Pari-Mutual Tax</u>. Section 73 eliminates the pari-mutuel tax economic development credit and earmarks 50 percent of the resulting receipts to the state fair for capital improvement projects other than improvements to the casino and racetrack. Remaining revenues are distributed to the general fund. Effective date: March 1, 2004.

<u>Regulatory Fees on Promotions</u>. Sections 74 through 79 deal with fees on athletic promotions. Section 74 strikes the 4 percent privilege tax on promotions and replaces it with a regulatory fee. The fee is to be established at an amount that covers the cost of regulating the contest, with a maximum set at four percent of total gross receipts. Section 75 directs regulatory and supervisory fee revenues to the athletic commission fund. Section 77 strikes the five percent tax on exhibiting live professional contests on closed-circuit telecast or motion picture. It replaces the tax with a "supervisory fee" in amount necessary to cover the cost of supervising the exhibition, but capped at five percent of gross receipts. Effective date: July 1, 2004.

<u>Tribal Agreements on Tribal Contests</u>. Section 80 allows the athletic commission to enter into a cooperative agreement with Indian nations, tribes and pueblos for the reciprocal, joint or common direction management or control of professional contests in New Mexico. Such agreements must be signed by the governor. Money collected by the commission on behalf of the Indian nation, tribe or pueblo is governed by the terms of the agreement. Effective date: July 1, 2004.

<u>Tax Identification Cards</u>. Section 81 modifies the tax identification card system by requiring TRD to issue annually original tax identification cards in sufficient for the number of motor vehicles specified by each motor carrier. Issuance of the card is contingent upon the motor carrier being in compliance with weight distance tax and special fuel user permit requirements. Effective date: July 1, 2004.

<u>Motorcycle Registration Fees</u>. Section 82 increases the twelve-month motorcycle registration fees from $11 to $15. Effective date: March 1, 2004.

<u>Passenger Vehicle Registration Fees</u>. Section 83 raises passenger vehicle registration fees. The fee for a vehicle weighing less than 2,000 pounds that has been registered for five years or less is increased from $20 to $27; registration fees on vehicles registered for more than five years in this weight class increase from $16 to $21. The fee for vehicles that weigh between 2,000 and 3,000 pounds and are five years old or less is increased from $29 to $39; the registration fees on vehicles in this weight category that have been registered for more than five years is increased from $23 to $31. The registration fee for vehicles that weigh more than 3,000 pounds and have been registered for five years or less is increased from $42 to $56; the registration fees on vehicles in this weight category that have been registered for more than five years is increased from $34 to $45. Effective date: March 1, 2004.

Trailer Registration Fees. Section 84 increases the registration for freight trailers from $10 to $13. The fee for utility trailers not permanently registered is increased from $5 plus one dollar for each 100 pounds in excess of 500 pounds to $7 plus one dollar for each 100 pounds in excess of 500 pounds. The permanent registration fee for utility vehicles not used in commerce is raised from $25 plus $5 for every 100 pounds above 500 pounds to $33 plus $7 for every 100 pounds above 500 pounds. Effective date: March 1, 2004.

Truck, Truck Tractor, Road Tractor and Bus Registration Fees. Fees for these vehicles vary by weight. Section 85 increases fees on vehicles weighing less than 4,000 pounds from $30 to $40. Registration fees on heavier vehicles are also increased by 33 percent. The rate on the heaviest vehicle—those over 48,000 pounds—is increased from $129.50 to $172. The percentage of truck fee revenues flowing to the tire recycling fund are reduced such that the fund continues to receive the same amount of money it would have prior to the change. Effective date: March 1, 2004.

Bus Registration Fees. Buses other than school buses and buses operated by religious and non-profit organizations pay the same registration fee as trucks. Section 86 increases the bus registration fee for school buses and religious and non-profits from $5 to $7. Effective date: March 1, 2004.

Registration Fees for Buses Used to Transport Agricultural Workers. Section 87 increases the registration for buses used exclusively to transport agricultural workers from $25 to $33. Effective date: March 1, 2004.

Fertilizer Trailers. Section 88 increases the registration fee for fertilizer trailers $5 to $7. Effective date: March 1, 2004.

Manufactured Home Fees. Section 89 increases the fee for the registration of manufactured homes from $5 to $7. Effective date: March 1, 2004.

School Bus Fees. Section 90 increases the registration fee for school buses from $5 to $7. Effective date: March 1, 2004.

Distribution of Registration Fees. Section 91 adjusts fee revenue distributions so that incremental road fund revenue flows to the road fund and other beneficiaries are held harmless. Effective date: March 1, 2004.

Overweight and Oversized Permit Fees. Section 92 increases oversize permit fees from $60 to $300 per year. Overweight permit fees, which are imposed on vehicles weighing more than 86,400 pounds, are raised from $15 for a single trip to $25 plus 4 cents for each ton mile. The Department of Public Safety is allowed to provide rules governing the times during which oversized and overweight vehicles or loads may be operated. Oversized and overweight permit revenues are distributed to the state road fund. Effective date: July 1, 2004.

Highway Projects Infrastructure. Sections 94 through 99 of the legislation authorize the New Mexico Finance Authority (NMFA) to issue $1.585 billion of bonds, on behalf of the State Transportation Commission, to fund construction of 47 highways projects throughout the state, called Governor Richardson’s Investment Partnership (GRIP). Effective date: Upon signature with two-thirds vote; if not February 2004.

Highway Infrastructure Fund. Section 94 amends the statute creating the highway infrastructure fund by including authority to use its dedicated revenue for GRIP projects, as identified in Sections 97 and 98 of this bill.

Transportation Bonds. Section 95 defines the financing strategy for GRIP projects.

Section 95a authorizes the State Transportation Commission to direct and pay NMFA to issue bonds on its behalf.

Section 95b provides a $1.585 billion limit on bond issuance for GRIP.

Section 95c authorizes NMFA to restructure existing bonds by exchange or current or advance refunding options.

Section 95d authorizes NMFA to define the terms, conditions and covenants of bond issue and provides discretion to NMFA to enter into financing strategies in addition to traditional fixed-rate structures. Requires project design life to meet or exceed bond maturities. It exempts NMFA issued bonds from Board of Finance approval.

Sections 95e, 95f, 95g, 95h provide standard language for issuance of tax-exempt bonds with a non-impairment clause to ensure the executive or legislature will not divert revenues in state road fund or highway infrastructure fund to other obligations until debt service is paid off, and allows bond proceeds to be used to pay bonds issuance costs.

Section 95i requires NMDOT to acquire highway construction materials from state lands, if feasible.

Section 95j requires bonds to be repaid from unobligated federal or state transportation revenues.

Section 95k defines state transportation project bonds by excluding those defined under Section 67-3-72, which includes revenue bonds payable solely out of the net income to be derived from the operation of the project, such as toll roads or bridges.

State Road Fund Distribution. Section 96 authorizes state treasurer to divert road revenue for payment of debt service on new transportation bonds prior to deposit in the road fund.

Appropriation of Bond Proceeds. Section 97 authorizes issuance of $1.585 billion of bond proceeds to be used to construct 47 projects and to improve NMDOT facilities. It requires the NMDOT and NMFA to present the detail of the proposed bond issuance to joint hearing of the NMFA Oversight and Legislative Finance Committees within 30 days of commission authorization for a bond sale. It requires unexpended or unencumbered amounts to revert to the state road fund.

Appropriation of Bond Proceeds—Matching Funds. Section 98 authorizes issuance of $12 million of bonds for two projects in the Albuquerque area, but requires a local funding match (from those local governments who benefit from the projects) to cover the remaining construction cost of these projects. The commission will be required to promulgate rules defining how the local match will be apportioned among the several entities impacted.

Temporary Provisions. Section 99 provides language to ensure existing bond debt is not impaired by the new issuance.

Repeals. Section 100 repeals requirement for each power unit to pay a $5.00 annual administrative fee.

Applicability Dates. Sections 24 through 30 apply to taxable years beginning on or after January 1, 2004.

Effective Dates. The effective date for sections 17, 45, 46, 48, 56, 71, 73, 82 through 91 is March 1, 2004.

The effective date for sections 11, 16, 18 through 23, 32 through 34, 36 through 38, 42 through 44, 47, 49 through 55, 72, 74 through 81, 92, 93, and 100 is July 1, 2004.

The effective date for provisions of section 35 is January 1, 2005.

The effective date of the provisions of sections 10, 12, 13, 14, 15, 31, 39, 40, 41, and 57 through 70 is July 1, 2005.

Emergency Clause. The act takes effect immediately.

SIGNIFICANT REVENUE ISSUES

Streamlined Sales Tax. The Blue Ribbon Tax Commission (BRTC) proposal adopted a provision allowing the state to enter the streamlined sales initiative discussions with other states. Participating provides the state a seat at the table; it would have a couple of years to determine whether it wanted to formally enter into the agreement. This initiative could eventually lead to the state being able to collect revenue from internet sales. Entering into the agreement would require legislative action.

Distribution of Liquor Excise Tax. Distributions to local governments are at least partially provided to ensure that the overall fiscal impact for local government from this bill is relatively neutral. TRD has estimated the distributional impacts for counties and municipalities. These are shown in **Appendix 1**.

Tax Administrative Issues. The fiscal impact of reducing the interest rate on tax delinquencies will be higher in later years. In FY07, the rate is reduced to the IRS rate, which corresponds to market interest rates. This could increase the cost in those years to more than $5 million.

Tax Exemption on Income of Persons 65 and Older. The benefit from this reduction is targeted to those persons with income too high to qualify for the current exemption.

Income Tax Filing Categories Reduced. According to TRD, this provision would provide tax relief to 13,000 of the 140,000 families filing taxes under the head of household option. Families in this category pay higher income taxes than two-parent families.

Low Income Tax Rebates. The BRTC recommended changing the name to FAIR and increasing rebate amounts as a means of targeting relief against gross receipts taxes on food to low and moderate income families, particularly large families. The rebates are increased to a level sufficient to offset food taxes.

Additional Income Tax Exemptions. The BRTC recommended increasing income tax exemptions for low and moderate income persons and families as a means of providing income tax relief for income groups that did not benefit from the income tax cut passed in last year's session.

Business Services Tax Credit. This tax aims at providing relief against the pyramiding involved in the gross receipts tax. Pyramiding is the payment of tax on a base that includes other previously paid taxes. It is of concern because it puts New Mexico businesses that are operating in a national market at a competitive disadvantage compared with out of state competitors. Unlike other proposals, however, this proposal does not target exporting business for relief. The credit is refundable, meaning that firms can claim it even if they had no gross receipts, compensating or withholding tax liabilities. TRD has noted that refundable credits could be challenged under the anti-donation clause.

Gross Receipts Tax Exemption for Certain Athletic Contests, Sporting Events and Concerts. TRD notes that this exemption may level the playing field for venues competing with Indian pueblos and tribal lands that also host such activities.

High Wage Tax Credit. The fiscal impact reported in the table reflects TRD assumptions on how many high wage jobs would be created. This estimate is based on information regarding the number of such jobs created in a recent year. Economic forecasts suggest that the state may experience stronger job growth in the future. Also, an assumption that the jobs created will be similar to activity in a prior year (which may be quite accurate given all the uncertainty) implies that the incentive does not result in additional jobs being created. Should the incentive prove effective, the fiscal impact (reduced general fund revenues) would be higher.

Gross Receipts Deduction for Receipts from Services Provided by Licensed Health Care Practitioners. The proposed change would result in different treatment of Medicaid HMO's and commercial HMO's. There is concern that this may become an issue with the federal Medicaid authorities.

Compensating Tax on Out of State Services. TRD's fiscal impact estimate in FY05 is $10 million. This increases to $15 million in FY06 as TRD anticipates greater knowledge and compliance with the change. The $15 million estimate is based on the assumed tax base. There is some risk that this additional revenue may not be realized, especially absent additional auditing resources. An additional concern is that the ramping up of revenue from this source coincides with a reduction in the effective tax rate for the state. This is because in FY06 a half percent municipal credit is implemented.

Motor Vehicle Tax Exemption. The fiscal impact of this legislation is relatively muted in near future. Technological breakthroughs could make such cars more competitive and available later on, however. A sunset provision may be in order. TRD suggests another alternative to dealing with the risks would be to provide a cap on the value of the exemption.

Weight Distance Tax Rates. NM DOT notes that these taxes have not been adjusted in twenty-years, and while the proposal is to increase the tax by 42 percent, inflation over that period eroded the purchasing power of the tax by more than 70 percent. They also note that 75 to 80 percent of the tax is exported to out-of-state businesses. It should be noted, however, that many states don't impose a weight distance tax.

Weight Distance Tax Identification Permits. Reform of the permitting process is critical to TRD ability to successfully administer the associated tax. Increased weight distance taxes are unlikely to provide additional revenue without better enforcement.

Liquor Excise Tax Rates. TRD reports that New Mexico rates on alcohol are already near the highest in the nation (**see Appendix 2**). For example, the wine tax rate is second only to Florida. Tax increases limited to New Mexico alone may lead to cross border driving for cheap alcohol, and a black market in bootlegged alcohol. The industry has also expressed concern about potential losses to internet sales, particularly sales of wine. On the positive side, the National Bureau for Economic Research has reported positive impacts of alcohol prices on drinking and driving and alcohol related accidents. They also report beneficial impacts on violent crime and some health indicators.

Severance Tax Rates on Oil Production. TRD provided a table (**see Appendix 3**) comparing New Mexico taxes on the oil and gas industries with those of other major producing states. The table shows that New Mexico's taxation of oil and gas is comparable to other states'. The proposed increase does not appreciably alter the comparisons.

Regulatory Fees on Promotions. According to RLD and TRD the proposed fee changes, which are designed to generate less revenue than the current tax, could impair the Athletic commission's ability to generate sufficient revenues to cover costs, including the cost of administration. RLD recommends increasing the regulatory fee to five percent.

Motor Vehicle Registration Fees. NM DOT reports that New Mexico registration fees are relatively low compared with other states. Compared to seventeen western states, New Mexico has the fifth lowest registration fee for passenger vehicles. The average registration fee for this group of states is $33.74.

SIGNIFICANT TRANSPORTATION, ROAD FUND AND BOND FINANCE ISSUES.

Based on bonding authority and new revenues in SB5, the NMDOT proposes to allocate approximately $45 million per year to debt service (principal and interest payments) for GRIP with the balance to the state road fund operating budget. The proposal raises the following issues, which are reviewed more completely in the fiscal implications section:

1. Several revenue options were eliminated from consideration at administration's direction.
2. Operating budget is falling behind as debt obligates larger share of operating revenue.
3. New revenue may not be sufficient to pay for GRIP spending.
4. GRIP requires restructuring of existing debt by lengthening maturities of bonds.
5. GRIP increases total debt from $1.3 billion to almost $4 billion.
6. GRIP eliminates bond capacity for the next 20 years.
7. GRIP bonds for rehabilitation projects and low-volume overlays.

FISCAL IMPLICATIONS BY FUND AND GOVERNMENT ENTITY

The Fiscal Implications are summarized in table below.
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FISCAL IMPLICATIONS FOR ROAD FUNDING

Based on its current revenue, NMDOT faces severe fiscal constraints as operating and construction costs have increased and revenues into the state road fund have stayed relatively flat. The current fiscal picture requires the administration and Legislature to consider new revenue options for NMDOT. According to the department, new revenue requirements total $75 million annually, at a minimum:

Debt Service for GRIP	$50 million
Fortify Operational Budget	$25 million

Revenue Options Eliminated. The Executive created a working group to assess the impact of the Native American gasoline tax exemption, while a Blue Ribbon Tax Commission assessed opportunities for increases to transportation-related taxes. The Native American gasoline tax exemption, which according to NMDOT represents a $15 million loss annually to the road fund, was recommended by the Executive working group to remain unchanged. In addition, the Executive spoke publicly about its unwillingness to support any increase in the gasoline tax[1], despite New Mexico's lower-than-surrounding-states rate:

State	Gas	Diesel
Arizona	$0.18	$0.26
Colorado	0.22	0.205
New Mexico	**0.185**	**0.195**
Texas	0.20	0.20
Utah	0.245	0.245

Incremental revenue in SB5 is targeted at heavy road users. According to NMDOT, 75 percent of the diesel truck traffic originates outside of and passes through New Mexico; 1 commercial vehicle weighing 80,000 pounds has as much impact on highways as does 38,000 motor vehicles.

Operating Budget Needs. The department typically holds as many as 400 staff positions vacant. Since FY03, the state-supported construction program, reflecting 3,000 miles of road, has not been funded. Meanwhile, according to agency officials, construction costs increase at a 4.5 percent inflation factor and the unit-based gasoline tax continues to lose its value when adjusted for inflation. The incremental road fund revenue would allow the department to boost maintenance and construction activities and fill needed positions.

Bonding Capacity Based on New Revenue. Bond experts typically use a 1-to-10 rule-of-thumb to determine bond capacity. Given incremental revenue in SB5, NMDOT could acquire approximately $500 million in principal. The department proposes two additional financing strate-

[1] The gas tax represents 35 percent of revenue in the state road fund. A one-cent increase reflects $8.4 million in new revenue, of which NMDOT receives approximately $6.5 million.

gies to achieve its $1.585 billion goal to fund GRIP:

1. Restructure existing 12-yr debt into 20-yr maturities, providing $122 million for new debt.
2. As bonds are paid off, use freed up cash for additional leverage.

Under these conditions, it is feasible to acquire the debt proposed by GRIP. To support this conclusion, NMFA ran several scenarios for the LFC, as shown in the table below:

Borrowing Amount Based on New Revenue (000s)

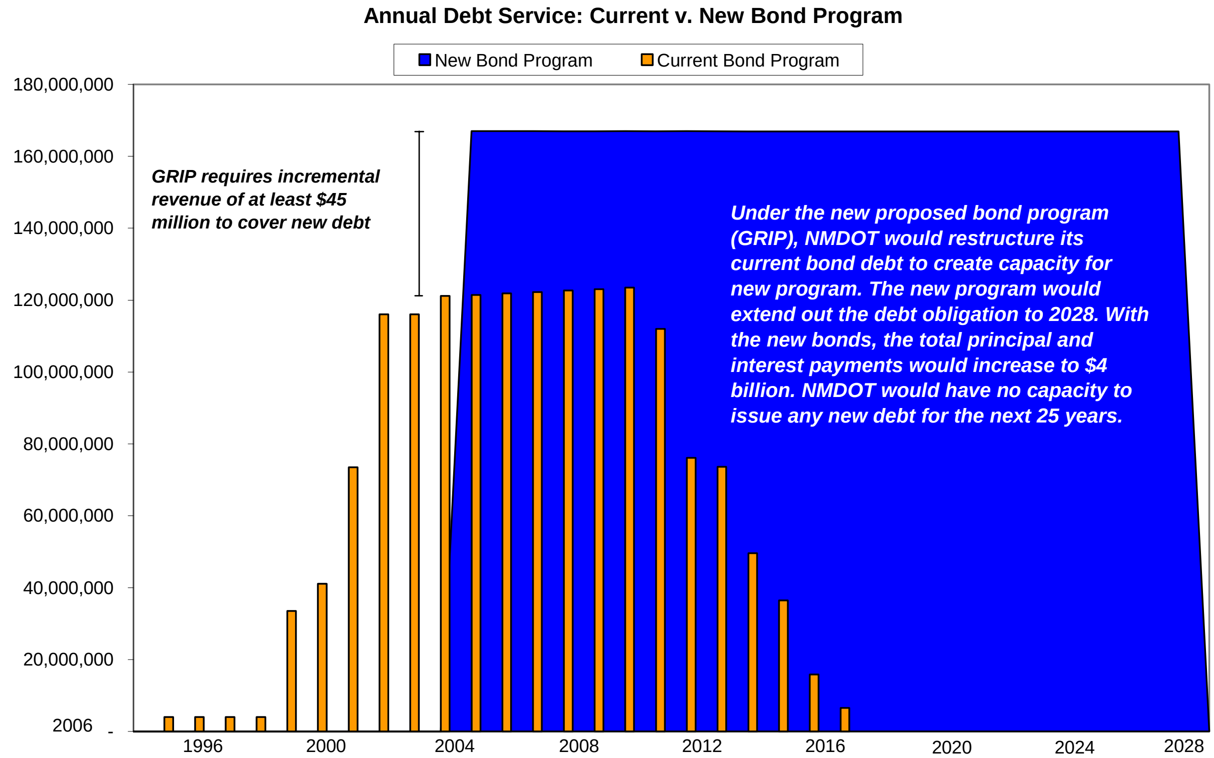
New Revenues	12-yr Maturity	16-yr Maturity	18-yr Maturity	20-yr Maturity
No new money	-	800,000.0	815,000.0	875,000.0
$25 million	625,000.0	1,100,000.0	1,260,000.0	1,350,000.0
$40 million	1,030,000.0	1,390,000.0	1,490,000.0	1,590,000.0
$45 million	1,160,000.0	1,470,000.0	1,578,000.0	1,670,000.0

These scenarios portray the total bond capacity, based on a given revenue source and maturity period. According to NMFA, this scenario would increase total debt to $4 billion, as shown in a similar table below.

Total Principal and Interest Payments for GRIP (Highway Construction)
Existing Principal and Interest Payments is $1.3 billion

New Revenues	12-yr Maturity	16-yr Maturity	18-yr Maturity	20-yr Maturity
No new money	$2.2 billion	$2.7 billion	$2.9 billion	$3.2 billion
$25 million	$2.1 billion	$3.2 billion	$3.5 billion	$3.8 billion
$40 million	$2.7 billion	$3.6 billion	$3.9 billion	$4.2 billion
$45 million	$2.9 billion	$3.7 billion	$4.0 billion	$4.3 billion

The following graphic compares the principal and interest proposed in GRIP with the current bond program payments. The annual payments would increase to a steady level of $170 million at least through the next two decades. The capacity to take on new debt would be virtually eliminated for the next 25 years.

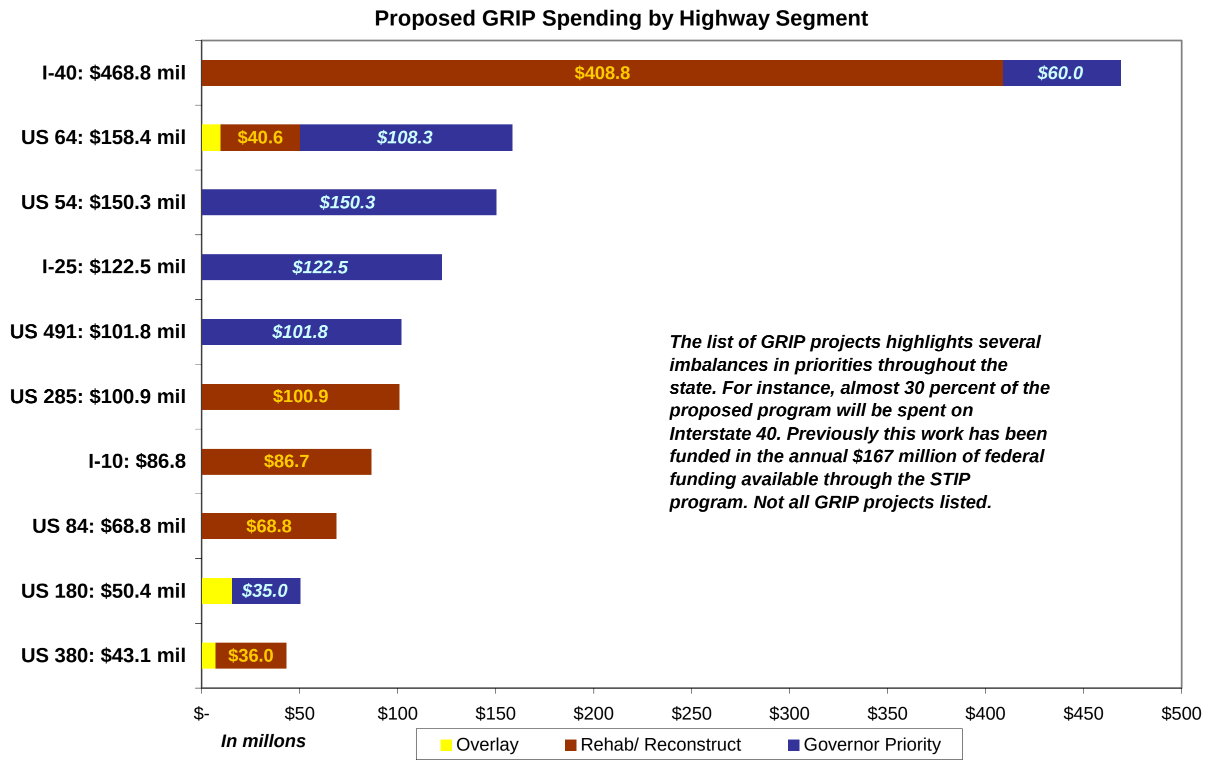


<u>Operating Budget Condition with GRIP</u>. **Appendix 4** shows an LFC forecast of the NMDOT operating budget over the next 20 years with GRIP. Using a 2 percent growth factor for revenues and expenditures, the simulation indicates, within four years, the annual debt service payments force a reduction in the rest of the operating budget, which is compounding for the remaining 20 years.

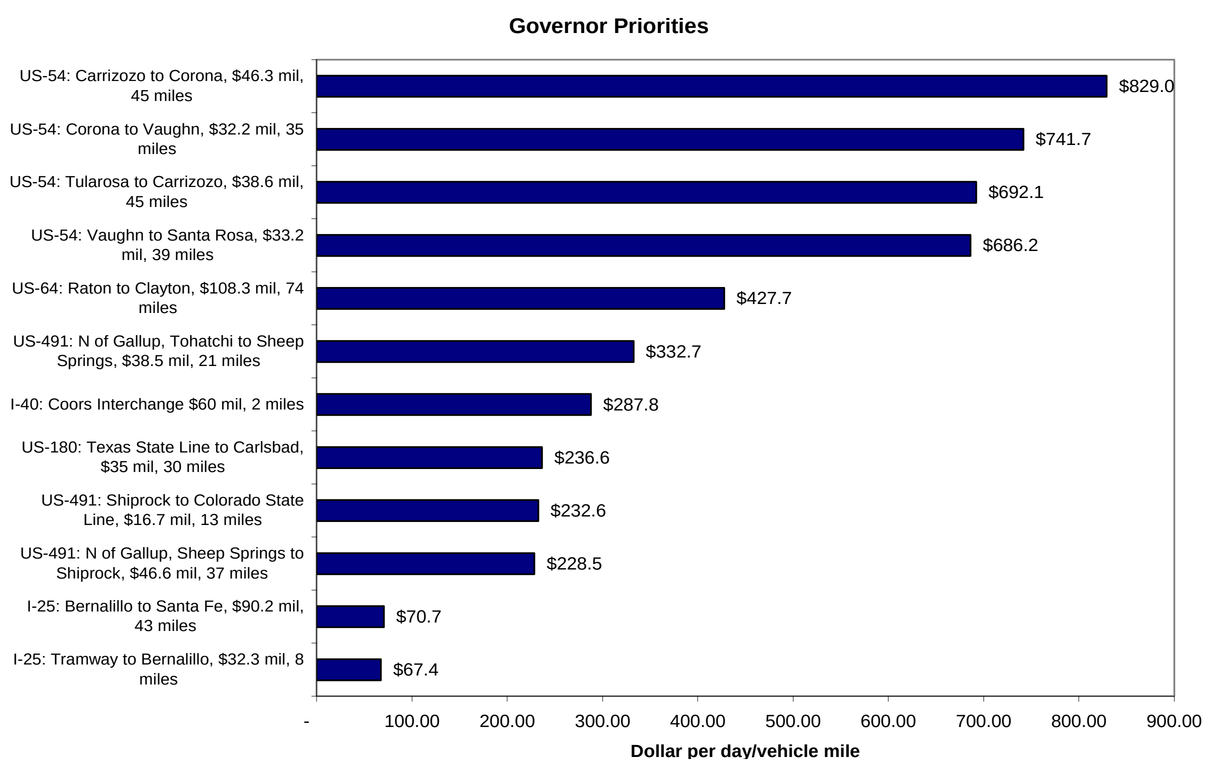
<u>GRIP Project Selection and Prioritization</u>. In collaboration with its District Engineers, NMDOT formulated the GRIP list from more than of $11.4 billion of unfunded transportation needs throughout the state. GRIP reflects the immediate, critical priorities, according to NMDOT. The methodology used by LFC to analyze the proposed project list was first to categorize these projects into the following three groups:

Governor's Top Priorities:	$	577.8 million
Reconstruct/Rehabilitation:	$	901.9 million
Overlay Projects:	$	63.6 million

The graphic which follows displays the total amount of GRIP funding dedicated to each highway segment. As shown, GRIP proposes spending almost 30 percent of the funding for Interstate 40. The need is unquestioned. However, NMDOT is funded by the federal government to manage interstate maintenance and rehabilitation through an annual program called the statewide transportation improvement plan (STIP). STIP, a 6-yr plan, is funded from dedicated federal funds of $167 million/year. Aside from the imbalance of funding for I-40, some GRIP projects duplicate planned STIP projects. As an example, one GRIP project would reconstruct US54 from Tularosa to Santa Rosa for $150 million. The project duplicates three stretches programmed under the STIP. It may be that STIP funding could cover some portion of the project cost.



One other concern is the prioritization of low-volume roads over higher-volume roads. A good example is seen between the $150 million for US 54 and $101 million for US 491. As the following graphic shows, US 491 has significantly higher traffic volumes and lower construction cost. This highway is also one of New Mexico's most dangerous.



Two additional graphics in **Appendix 5**, display the results of this analysis for the rehabilitation and overlay projects.

One final concern about the GRIP program is the proposal to bond for low-volume maintenance work. The third category represents 11 overlay projects, i.e., projects traditionally with useful lives of 5 to 7 years. SB5 contains language requiring NMDOT to design the project life to meet or exceed the bond maturity. However, these projects could be accommodated through either the annual STIP program or through a fully funded state construction program. Issuing long-term debt for short-term maintenance projects simply exacerbates the declining quality of the transportation. The concern is applicable to several projects in the rehabilitation/reconstruction category.

TECHNICAL ISSUES

LFC notes a technical issue in Section 96, page 180. The section refers to "state transportation revenue bonds," which is contrary to the specific term of "state transportation project bonds" used in the previous section. In fact, state transportation revenue bonds have a specific meaning, which refers to bonds financed from the net income of transportation projects.

OTHER SUBSTANTIVE ISSUES

SB5 provides substantial flexibility to NMDOT and NMFA in specifying priorities and allocating bond proceeds for these projects. Furthermore, NMFA has considerable discretion in designing the financing strategy for the bond sales and is not required to receive Board of Finance approval. One provision of SB5 requires NMFA and NMDOT to present details of the bond sale to the NMFA Oversight and Legislative Finance Committees. However, these committees have no approval authority over the details. As an option, the Legislature may want to consider tying bond proceeds to specific projects.

Due to accounting changes impacting the timing of revenue recognition (i.e., GASB 34 issue), general fund reserves are now estimated to be more than $500 million, or 12 percent of recurring expenditures in FY04. This may provide an opportunity to partially draw down on those reserves for non-recurring expenditures, such as state road infrastructure projects.

Continuing Appropriations

This bill, in Section 94, diverts incremental revenue to the highway infrastructure fund and provides for continuing appropriations. The LFC objects to including continuing appropriation language in the statutory provisions for newly created funds. Earmarking reduces the ability of the legislature to establish spending priorities. The Legislature may want to add the following language:

> Money in the highway infrastructure fund shall be appropriated by the legislature for specific highway construction projects.

BT/SN/MV/yr