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FISCAL IMPACT REPORT

ORIGINAL DATE 2/18/07
 LAST UPDATED 2/24/07 HB _____

SPONSOR Cisneros

SHORT TITLE Electric Power Plant Property Valuation SB 874

ANALYST Francis

REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Non-Rec	Fund Affected
FY07	FY08	FY09		
	* See Narrative			

(Parenthesis () Indicate Revenue Decreases)

Duplicates HB666
 Relates to HB665, SB340

SOURCES OF INFORMATION

LFC Files
 Taxation and Revenue Department (TRD)

Response Received From
 Taxation and Revenue Department

SUMMARY

Synopsis of Bill

Senate Bill 874 modifies the valuation methodology for property used in the generation, distribution or transmission of electricity. The valuation can include deductions for “functional” and “economic” obsolescence.

- Economic obsolescence is defined as the loss of value caused by unfavorable economic influences or factors outside of the property not including physical depreciation.
- Functional obsolescence is loss due to functional inadequacies or deficiencies caused by factors within the property not including physical depreciation.

The taxpayer choosing to include economic and/or functional obsolescence must submit a claim documenting the obsolescence. Such documentation may include industry comparisons, volume reductions, and other objective evidence of obsolescence. The Taxation and Revenue

Department (TRD) will determine if the evidence is sufficient and notify the taxpayer if a claim is rejected with the reasons and what additional information is needed to establish obsolescence, giving a taxpayer enough time to comply.

A taxpayer is given a choice of valuation methods:

1. capitalization of income
2. market value of stock
3. cost less allowance for obsolescence and depreciation.

Whichever method chosen the taxpayer must use that method for subsequent years unless, after three years, the taxpayer can show sufficient cause to change methods.

This act is applicable to property tax years 2007 forward.

FISCAL IMPLICATIONS

There is no significant general fund impact though there may be significant impacts in counties where there are electrical generating plants. There is no precise way to determine the impact of this modification to the valuation methodology. Since there is a choice of methods, the likely result is that property valuation will be lower in the future.

If assessed values do decrease as a result of this change, the impact depends on what the affected county requires from property tax collections. If the county requires the revenue prior to this change in valuation, rates for all property taxpayers will rise or fall to compensate for the change in valuation. The county could keep the rates the same and the impact would come from tax collections.

ADMINISTRATIVE ISSUES

TRD reports that they would need an additional FTE at \$65,000 to manage an estimated five additional unitary valuations per year.

ALTERNATIVES

TRD:

Proposed Amendments: 1) insert an emergency clause into the proposal, 2) delete sections of the proposal allowing taxpayers an election to be assessed using unitary appraisal methods, and 3) specify that an electric plant may not be valued at a higher “level than ‘tangible property cost’ less the appropriate straight-line depreciation over the economic life of the property”. In cases where the Department disputes an investor-owned utility’s claim for functional or economic obsolescence, however, the claims may be adjudicated by use of unitary appraisal methods based on 1) one-third capitalization of earnings; 2) one-third market value of stock and debt; and 3) one-third cost less depreciation, economic and functional obsolescence.

OTHER ISSUES

TRD:

Unitary Assessment, Functional and Economic Obsolescence

The unit rule of appraisal is defined as "...an appraisal of an integrated property as a

whole without reference to the value of its component parts. The approach is based on a view that informed buyers and sellers purchase or sell a viable operating unit, rather than portions of the property. This procedure incorporates "going concern" value associated with a customer base, as opposed to a new customer base a firm would need to develop if it purchased only portions of an established business. The unit rule may be applied appraisals based on the cost approach, comparable sales approach or income approach.

As indicated above, the cost approach to appraisal estimates market value by making a series of adjustments to estimates of replacement cost, including allowances for economic and functional obsolescence. The sales comparison approach essentially appraises property by comparing the property to prices of similar properties that have recently sold – with appropriate adjustments. The income approach estimates the amount of money a typical purchaser would pay for a (typically income-producing) property based on the income generating ability of the property.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

SB 874 relates to HB665 and SB340 as far as proposing to use functional and economic obsolescence as a factor for valuation. SB 874 refers to electrical transmission property where the other two bill refer to oil and gas transmission property. HB 666 is a duplicate of SB874.

NF/mt