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## FISCAL IMPACT REPORT

ORIGINAL DATE 2/15/17

SPONSOR Padilla LAST UPDATED \_\_\_\_\_ HB \_\_\_\_\_

SHORT TITLE Taxes & Surtaxes for Early Childhood SB 288

ANALYST Iglesias

### REVENUE (dollars in thousands)

Estimated Revenue					R or NR **	Fund Affected
FY17	FY18	FY19	FY20	FY21		
\$0	\$871.9	\$884.5	\$922.8	\$960.2	Recurring	NEW Early Childhood Education Fund (from oil and gas emergency school surtax)
\$0	\$326,955.5	\$323,161.8	\$325,203.4	\$325,106.9	Recurring	NEW Early Childhood Education Fund (from electricity production tax)

Parenthesis ( ) indicate expenditure decreases. \*\* R = recurring; NR = non-recurring

### SOURCES OF INFORMATION

LFC Files

#### Responses Received From

Energy, Minerals, and Natural Resources Division (EMNRD)  
Children, Youth and Families Department (CYFD)

#### Responses Not Received From

Taxation and Revenue Department (TRD)

### SUMMARY

#### Synopsis of Bill

Senate Bill 288 imposes an “oil and gas emergency school surtax” of 0.01 percent on producers severing oil, natural gas, carbon dioxide, liquid hydrocarbons, helium, and non-hydrocarbon gases in the state. The bill also levies a privilege-to-do-business tax of 1 cent per kilowatt hour (kWh) on all electricity produced in the state for sale or trade. Exemptions from the electricity production tax are created for electricity produced by the federal government, the State of New Mexico, activities and transactions on sovereign Indian territory, and foreign nations where applicable by U.S. treaty. The tax also does not apply to individuals generating less than 500 kWh of electricity for personal consumption per 24-hour period.

The bill also creates an “early childhood education fund” and distributes all revenues generated from the oil and gas emergency school surtax and the electricity production tax to this fund. Funds are intended to supplement, not supplant, existing revenue sources for early childhood education, and money in the fund will not revert to the general fund at the end of a fiscal year.

The early childhood education fund will be administered by the Children, Youth and Families Department (CYFD) and may be used for the following purposes:

1. To provide early childhood education to children from birth to age five;
2. For curriculum development and materials for early childhood education; and
3. To improve the quality of the provision of early childhood education.

The provisions of the bill apply to products severed and sold beginning on and after July 1, 2017, and to the production of electricity beginning on and after July 1, 2017.

### **FISCAL IMPLICATIONS**

This bill distributes all revenues from both the oil and gas emergency school tax and the electricity production tax to the early childhood education fund. The two revenue sources combined provide over \$320 million annually to the newly created early childhood education fund.

The fiscal impact of the oil and gas emergency school surtax is calculated by applying the 0.01 percent tax rate to the oil and natural gas prices and volumes forecasted in the December 2016 consensus revenue estimate, as well as carbon dioxide prices and volumes forecasted based on a two-year moving average using data from ONGARD. Based on this methodology, the surtax is expected to generate revenues of \$872 thousand in FY18 and to grow moderately each year thereafter.

Data from the U.S. Energy Information Administration (EIA) on electricity generation in New Mexico is used to calculate the fiscal impact of the electricity production tax. New Mexico generated 33.8 terawatt hours (TWh) of electricity in FY14, 31.7 TWh in FY15, and 32.5 TWh in FY16, across the total electric power industry (including natural gas, petroleum, coal, and renewable energy sources).<sup>1</sup> A 1-cent tax levied on these totals results in revenues ranging from \$317 million to \$338 million. The fiscal impact estimate uses a three-year moving average to estimate megawatt hour generation and corresponding tax revenues in fiscal years 2018-2021.

The chart below shows the revenues that would be generated from each industry based on FY16 production levels.

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<sup>1</sup> One terawatt hour (TWh) is equal to 1 million megawatt hours (MWh) and equal to 1 billion kilowatt hours (kWh).

<b>Electric Power Industry</b>	<b>New Mexico Electricity Generation (MWh)*</b>	<b>Estimated Revenue – 1 cent per kWh (dollars)</b>
Coal	18,764,217	\$ 187,642,171
Geothermal	14,208	\$ 142,080
Hydroelectric Conventional	141,352	\$ 1,413,518
Natural Gas	9,881,270	\$ 98,812,696
Other	424	\$ 4,240
Other Biomass	16,162	\$ 161,619
Petroleum	56,421	\$ 564,210
Solar Thermal and Photovoltaic	682,449	\$ 6,824,489
Wind	2,992,786	\$ 29,927,863
<b>Total Electric Power Industry</b>	<b>32,549,289</b>	<b>\$ 325,492,886</b>

Source: U.S. Energy Information Administration (EIA)

\*1 MWh = 1000 kWh; 1,000,000 MWh = 1 TWh

This bill creates a new fund and provides for continuing appropriations. LFC has concerns with including continuing appropriation language in the statutory provisions for newly created funds, as earmarking reduces the ability of the Legislature to establish spending priorities.

### **SIGNIFICANT ISSUES**

According to EIA, New Mexico retail sales in 2015 totaled 23.1 TWh from electricity full service providers and net generation of electricity in New Mexico in was 32.7 TWh.<sup>2</sup> New Mexico’s primary energy source for electricity is coal, and the average retail price of electricity in the state is \$9.62/kWh.

Because electric rates are designed to recover cost-of-services, including taxes, it is fair to say that the taxes imposed in this bill will likely be passed on to the consumer.

**Early Childhood.** The New Mexico PreK Program (Children’s Code, 32A-23-1-8) provides voluntary pre-kindergarten services to four-year-old children in the state. The program shall address the total developmental needs of preschool children including physical, cognitive, social and emotional needs and, also, health care, nutrition, safety and multicultural sensitivity. This bill provides a significant source of funding for early childhood education programs; however, it is unclear whether those funds could immediately be put to use toward those programs. Prior to this year’s budget shortfall, New Mexico PreK programs had relatively small waiting lists across the state. Additionally, only 54 of 89 school districts participate in the program.

LFC and other studies have shown early care and education services to increase school completion rates producing benefits of \$278 thousand for the graduate and \$100 thousand for taxpayers and other beneficiaries, compared with a non-graduate.

In the 2015-2016 school year, PED received \$24.5 million to fund PreK programs in school districts and charter schools, \$3.5 million of which was allocated from federal TANF (Temporary Assistance to Needy Families) funds. In that same year, CYFD received \$22.6 million (\$11.6 million in state general funds and \$11 million in TANF funds for New Mexico

<sup>2</sup> U.S. Energy Information Administration, State Energy Profiles, <https://www.eia.gov/electricity/state/newmexico/>

PreK programs. CYFD also received \$4 million (\$2 million in state general funds and \$2 million in TANF funds for New Mexico Early PreK programs.

Despite significant, targeted investments by the Legislature in the state’s early childhood programs, New Mexico remains behind most other states in many indicators of child well-being. LFC’s Gap Analysis and Spending Plan report (January 2015) examined home-visiting, prekindergarten, child care, and K-3 Plus for gaps in services, barriers to program expansion, and potential funding options. The gap analysis found enough publically funded slots for 4-year-old students exist to provide nearly all low-income 4-year-olds with some form of early childhood education, though many children currently served are not low-income. An estimated 27 thousand 4-year-olds live in New Mexico and 73 percent are low-income as measured by free or reduced-fee lunch status. Roughly 17,500 slots for 4-year-old early care and education programs are funded annually, including state funded prekindergarten, four and five star childcare, Head Start, and special education preschool. However, only 80 percent of participants in prekindergarten programs are low-income.

The response from the Children, Youth and Families Department (CYFD) did not address the agency’s plan to utilize resources from the early childhood education fund created by this bill.

## RELATIONSHIP

House Bill 191 also amends Section 7-1-6.20 NMSA 1978 by referencing new sections.

## OTHER SUBSTANTIVE ISSUES

Ohio created a kilowatt-hour tax in 2001 as part of a broader legislative effort to deregulate electric utilities. In Ohio, the tax applies to electric distribution companies with end users in Ohio and the rates vary according to the kilowatt-hour consumption of individual end users of electricity. The rates are substantially lower than rates proposed in this bill and are tiered as follows:

<b>Ohio Kilowatt Hour Tax Rates</b>	
<b>Monthly Kilowatt Hours Distributed to the End User</b>	<b>Rate Per Kilowatt Hour</b>
0 – 2,000 kWh	\$0.00465
2,001 – 15,000 kWh	\$0.00419
Over 15,001 kWh	\$0.00363

Does the bill meet the Legislative Finance Committee tax policy principles?

- 1. Adequacy:** Revenue should be adequate to fund needed government services.
- 2. Efficiency:** Tax base should be as broad as possible and avoid excess reliance on one tax.
- 3. Equity:** Different taxpayers should be treated fairly.
- 4. Simplicity:** Collection should be simple and easily understood.
- 5. Accountability:** Preferences should be easy to monitor and evaluate