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

		ORIGINAL DATE	1/24/22		
SPONSOR	Chandler	**LAST UPDATED**		**HB**	14
SHORT TITLE	Bonds & GRT Deduction For Electric Storage			**SB**	
				ANALYST	Graeser

REVENUE (dollars in thousands)

Estimated Revenue						Recurring or Nonrecurring	Fund Affected
FY 22	FY 23	FY24	FY25	FY26	FY27		
		Up to ($5,000.0)	Up to ($5,000.0)	Up to ($5,000.0)	Up to ($5,000.0)	Recurring	State General Fund (GRT)
		Up to (1,500.0)	Up to ($1,500.0)	Up to ($1,500.0)	Up to ($1,500.0)	Recurring	County (GRT)
			Small annual losses <(100.0) per project approved			Recurring	State -- GO Bond Levy
			Moderate annual losses <(500.0) for district with project			Recurring	School District
			Declining annual losses <(500.0)			Recurring	County -- Property Tax
			Level negotiated payments <500.0			Recurring	County – PILT
			Small positive or negative net of foregone property tax and PILT over the duration of the project			Recurring	County – Net

Parenthesis ( ) indicate revenue decreases

SOURCES OF INFORMATION

LFC Files: FIR for 2020's HB50 and 2021's HB105

Responses Received From
Energy, Minerals and Natural Resources Department (EMNRD)
Taxation and Revenue Department (TRD)

SUMMARY

Synopsis of Bill

House Bill 14 amends both the Municipal Industrial Revenue Bond Act and the County Industrial Revenue Bond Act to make renewable energy storage projects eligible for industrial revenue bond treatment. HB14 also amends the Gross Receipts and Compensating Tax Act to provide gross receipts tax deductions for sales of energy storage equipment to a governmental entity for the purposes of installing a renewable energy storage facility.

EMNRD has provided a section-by-section description:

> "Section 1 amends the Municipal Industrial Bond Act (Section 3-32-1. B (5) NMSA 1978) to include an energy storage facility as an eligible project."
>
> "Section 2 amends the County Industrial Revenue Bond Act (Section 4-59-2. F(4)(b) NMSA 1978) to include an energy storage facility as an eligible project."
>
> "Section 3 amends the Gross Receipts and Compensating Tax Act (Section 7-9-54.3 NMSA 1978) to add a gross receipts deduction for energy storage equipment sales to governmental entities. Additional text clarifies that energy storage equipment sold to a governmental entity must be for the purpose of installing a renewable energy storage facility."
>
> "'Energy storage equipment' is defined as "equipment that is installed for the purpose of storing electric energy received from a wind or solar electric generation facility that uses mechanical, chemical, thermal, kinetic or other processes to store energy for release at a later time and related equipment." Under "related equipment," HB14 adds, "power conversion equipment" and expands related equipment to cover both the connection of a wind and solar plan and a renewable energy storage facility."

The effective date of this bill is July 1, 2022. In the 2020 session, LFC recommended including a delayed repeal to HB50 (2020), but this recommendation was not adopted. The addition of electrical generating and transmission facilities, as well as this addition of energy storage facilities to the IRB act creates an unusual tax expenditure and a delayed repeal date would give the legislature an opportunity to review the success or failure of these proposals.

FISCAL IMPLICATIONS

Estimating the cost of tax expenditures is difficult. In this case, it remains uncertain exactly what the foregone revenue will be because of technical issues as well as the apparent fact that with or without the IRB provision, it is possible that no renewable energy storage facilities will be built within the five-year period for this analysis.

The provisions support the transition of the state's energy production to zero carbon by mid-century. This goal is achieved at the cost of both a non-recurring gross receipts tax impact for each project and a recurring property tax impact that is negative at the beginning and positive at the end for the sponsoring county. For the entire period, the state general obligation (GO) bond fund and the affected school district(s) will experience a revenue loss measured against current law.

This bill may be counter to the LFC tax policy principle of adequacy, efficiency, and equity. This bill creates a tax expenditure with a cost that is difficult to determine but likely significant. The LFC has serious concerns about the significant risk to state and local revenues from tax expenditures and the increase in revenue volatility from erosion of the revenue base. This particular tax expenditure affects county governments and school districts more than the state, although the abatement of gross receipts and compensating taxes would be significant for both the state general fund and county and municipal general funds. The revenue losses would depend strongly on uptake (the number of renewable energy systems installed pursuant to the provisions of the bill) and location of the installations.

As pointed out by TRD, the fiscal implications of the provisions of this bill are indeterminate, but likely to be significant.

IRBs are generally not financing tools, but tax abatement mechanisms. IRBs are built on an assumption that the tangible personal property involved in the IRB project is "owned" by the sponsoring government. Receipts from sales of tangible personal property to government can be deducted although gross receipts tax on construction materials and installation remain taxable. In this case, the bill contains an explicit gross receipts and compensating tax deduction that would apparently apply even if the renewable energy storage facilities would otherwise be considered as construction. In addition to the gross receipts and compensating tax impact, the bill provides property tax abatement. Both solar and wind renewable energy storage systems are considered as tangible personal property and valued at cost minus accumulated straight-line depreciation, with salvage value at 20 percent of cost. With the provisions of the bill, however, there would be no property tax on the renewable energy storage facilities because the project's working assets are considered to be owned by the sponsoring government. This treatment extends for the duration of the bonds – limited in statute to 30 years. In practice, the sponsoring county (or municipality) negotiates a payment-in-lieu-of-property-taxes (PILT), pursuant to the provisions of the bill, the state GO bond fund and the school districts in which the projects are located would be excluded from the PILT.

The analysis assumes that in the absence of the provisions of this bill, the renewable energy storage facilities would be considered as tangible personal property for the purpose of determining the probable property tax liability and as construction for the purpose of determining the probable gross receipts/compensating tax liability. Because the fiscal implications of this bill are largely indeterminate, LFC staff developed the following scenario-based exhibit which assumes a renewable energy storage system that will provide 4-hour backup of a 100 megawatt (MW) solar or wind farm and the cost will be $250 per installed kilowatt-hour (KwH). Thus the installed cost would be $100 million. In the exhibit, the project is located in an eastern New Mexico county and a single school district. However, this is an exhibit and actual uptake could be substantial and the costs to state and local governments could be significant. The estimated revenue for this exhibit is shown below.

Estimated Revenue						Recurring or Nonrecurring	Fund Affected
FY22	FY23	FY24	FY25	FY26	FY27		
		($5,170.0)				Non-Recur	State General Fund (GRT)
		($910.0)				Non-Recur	County (GRT)
		($610.0)				Non-Recur	County Hospital (GRT)
			($45.0)	($43.0)	($40.0) to ($9.0)	Recurring	State -- GO Bond Levy
			($310.0)	($293.0)	($277.0) to ($150.0)	Recurring	School District
			($395.0)	($374.0)	($353.0) to ($79.0)	Recurring	County -- Property Tax
			$214.0	$214.0	$214.0	Recurring	County – PILT
			($181.0)	($160.0)	($138.0) to $135.0	Recurring	County – Net

The gross receipts tax impacts are as follows:

	FY24	
	Location Portion Paid (Thousands	GRT Rate
County Unrestricted	($550.0)	0.5625%
County Fire	($120.0)	0.1250%
County Hospital	($610.0)	0.6250%
County Med	($240.0)	0.2500%
State General Fund (GRT/Comp)	($5,170.0)	5.1250%
Total	($6,690.0)	6.6875%
Source: Note: this exhibit includes the 3 percent administrative fee charged by TRD for all county gross receipts tax collections. These administrative fees are transferred to the general fund. The gross receipts tax impacts are shown as non-recurring since this is an exhibit assuming a one-time installation.		

Counties will likely lose revenue for the first nine years due to property tax losses and the PLT then gradually gain revenue while school districts will likely consistently lose a declining amount of property tax revenue. The counties may negotiate greater amounts of PILT than the exhibit indicates.

	FY 25	FY26	FY27	FY28	FY29	FY30	FY31	FY32	FY33
Depreciated Valuation (1/3rd tax ratio) ($ Millions)	$33.3	$31.6	$29.8	$28.0	$26.2	$24.4	$22.7	$20.9	$19.1
State -- GO Bond Levy	($45.0)	($43.0)	($40.0)	($38.0)	($36.0)	($33.0)	($31.0)	($28.0)	($26.0)
County -- Property Tax	($395.0)	($374.0)	($353.0)	($332.0)	($311.0)	($290.0)	($269.0)	($248.0)	($226.0)
County -- PILT	$214.0	$214.0	$214.0	$214.0	$214.0	$214.0	$214.0	$214.0	$214.0
County -- Net	($181.0)	($160.0)	($138.0)	($117.0)	($96.0)	($75.0)	($54.0)	($33.0)	($12.0)
School District	($310.0)	($293.0)	($277.0)	($260.0)	($244.0)	($227.0)	($211.0)	($194.0)	($178.0)
	($750.0)	($710.0)	($670.0)	($630.0)	($591.0)	($550.0)	($511.0)	($470.0)	($430.0)
	FY34	FY35	FY36	FY37	FY38	FY39	FY40	FY41	FY42
Depreciated Valuation (1/3rd tax ratio) ($ Millions)	$17.3	$15.6	$13.8	$12.0	$10.2	$8.4	$6.7	$6.7	$6.7
State -- GO Bond Levy	($24.0)	($21.0)	($19.0)	($16.0)	($14.0)	($11.0)	($9.0)	($9.0)	($9.0)
County -- Property Tax	($205.0)	($184.0)	($163.0)	($142.0)	($121.0)	($100.0)	($79.0)	($79.0)	($79.0)
County -- PILT	$214.0	$214.0	$214.0	$214.0	$214.0	$214.0	$214.0	$214.0	$214.0
County -- Net	$9.0	$30.0	$51.0	$72.0	$93.0	$114.0	$135.0	$135.0	$135.0
School District	($161.0)	($145.0)	($128.0)	($112.0)	($95.0)	($78.0)	($62.0)	($62.0)	($62.0)
	FY43	FY44	FY45	FY46	FY47	FY48	FY49	FY50	
Depreciated Valuation (1/3rd tax ratio) ($ Millions)	$6.7	$6.7	$6.7	$6.7	$6.7	$6.7	$6.7	$6.7	
State -- GO Bond Levy	($9.0)	($9.0)	($9.0)	($9.0)	($9.0)	($9.0)	($9.0)	($9.0)	
County -- Property Tax	($79.0)	($79.0)	($79.0)	($79.0)	($79.0)	($79.0)	($79.0)	($79.0)	
County -- PILT	$214.0	$214.0	$214.0	$214.0	$214.0	$214.0	$214.0	$214.0	
County -- Net	$135.0	$135.0	$135.0	$135.0	$135.0	$135.0	$135.0	$135.0	
Logan School District	($62.0)	($62.0)	($62.0)	($62.0)	($62.0)	($62.0)	($62.0)	($62.0)	
Note: The property tax exhibit assumes that the County negotiates a PILT that provides a net present value (NPV) over the 25-year assumed life of the level payment to be equal to the NPV of the depreciated cost basis of the $100,000,000 cost of the renewable storage system. In both cases, we used a 5% discount rate. The PILT was calculated at $241,000 per year.									

SIGNIFICANT ISSUES

The provisions of this bill support the transition of the state's energy production and consumption to zero carbon by mid-century. This goal is achieved at the cost of both a non-recurring gross receipts tax impact for each project and a recurring property tax impact that is negative at the beginning and positive at the end for the sponsoring county. For the entire period, the state GO bond fund and the affected school district(s) will experience a revenue loss measured against current law.

This bill could be considered as a technical addition to the successive amendments of the Industrial Revenue Bond Act adding utility scale wind farms, solar generation and associated transmission lines to that act. The addition in this bill is to add energy storage facilities to the list of allowed IRB projects. However, this bill's provisions do not contain a number of the provisions of 2020's HB50 and 2021's HB105 or of other reforms mentioned with regard to IRBs.

This bill narrows the gross receipts tax (GRT) base for both the state general fund and the affected counties' general and special purpose funds. Many of the efforts over the last few years to reform New Mexico's taxes focused on broadening the GRT base and lowering the rates. Narrowing the base leads to continually rising GRT rates, increasing volatility in the state's largest general fund revenue source. Higher rates compound tax pyramiding issues and force consumers and businesses to pay higher taxes on all other purchases without an exemption, deduction, or credit.

The bill does not contain provisions for sharing the in-lieu-of-property tax payments rendered pursuant to an IRB agreement with the adopting county or counties with the state (general obligation bonds) or school districts (operating levies and debt) as negotiated in previously enacted bills (see Conflict, Duplication, Companionship and Relationship section below). Also, local governments are eligible to receive compensating taxes at their local option GRT rate and would experience a decrease in revenue from this source pursuant to the provisions of this bill.

EMNRD contributed the following observations:

> HB 14 can be seen as a follow-up to 2002's HB 143, which added renewable energy projects, and 2020's HB 50, which added electric transmission line projects to the industrial revenue bond statutes. Those two bills and the proposed all support the growth of renewable energy in the state and help to ensure that local governments receive tax revenues from renewable projects sited in their jurisdictions.
>
> The main role of energy storage is to capture surplus energy when it is available to store it until it is needed – i.e., when electricity generation may not be sufficient to meet demand. Energy storage therefore increases the reliability and resilience of the electric grid. As New Mexico's electric grid decarbonizes, becoming more reliant on wind and solar generation (both of which are variable in availability), the installation of energy storage facilities will become increasingly important towards ensuring reliability and resilience.
>
> Energy storage is often co-located with renewable energy generation facilities. However, the current costs of energy storage equipment, particularly for longer-duration (more than four hours) storage, may be prohibitive for renewable generation developers if they must be borne by the developer outright. Industrial revenue bond eligibility for these projects will increase the likelihood that developers will choose to add storage to their construction plans. It will also give local governments financing tools enabling them to benefit from storage projects.

PERFORMANCE IMPLICATIONS

The LFC tax policy of accountability is <u>not</u> met since TRD is <u>not</u> required in the bill to report annually to an interim legislative committee regarding the data compiled from the reports

regarding taxpayers taking the deduction and the exemption and other information which would allow the Legislature to determine whether the deduction and exemption are meeting their purpose.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

The bill does not contain provisions for sharing of the in-lieu-of-property tax payments rendered pursuant to an IRB agreement with the adopting county or counties with the state (general obligation bonds) or school districts (operating levies and debt) as negotiated in 2020's HB50 and last year's HB105, which were both enacted. In addition, the bill provides for a state and local government gross receipts tax and compensating tax deduction for renewable energy storage equipment when sold to governments in an IRB transaction. This provision was not included in 2020's HB50 for electrical generation and transmission facilities. Because of 2019's HB6, local governments are eligible to receive compensating taxes at their local option GRT rate and would experience a decrease in revenue from this source pursuant to the provisions of this bill.

TRD notes that the following bills are precursors for HB14: similar HB262 (2021 Regular Session), SB301 (2021 Regular Session) Similar to HB201 (2020 Regular Session)

TECHNICAL ISSUES

In the absence of the explicit gross receipts and compensating tax deduction in Section 3 of the bill, the full amount of the costs of materials and labor would be considered construction and taxable, even though sold to an IRB-sponsoring governmental entity. The exemptions for this treatment would apply if the property were considered three-year, five-year, seven-year, or 10-year property as expressed in Section 7-9-54 NMSA 1978.

7-9-54 NMSA 1978. Deduction; gross receipts tax; governmental gross receipts tax; sales to governmental agencies.

> A. Receipts from selling tangible personal property to the United States or New Mexico or a governmental unit, subdivision, agency, department or instrumentality thereof may be deducted from gross receipts or from governmental gross receipts. Unless contrary to federal law, the deduction provided by this subsection does not apply to: …
> (3) receipts from selling construction material, excluding tangible personal property, whether removable or non-removable, that is or would be classified for depreciation purposes as three-year property, five-year property, seven-year property or ten-year property, including indirect costs related to the asset basis, by Section 168 of the Internal Revenue Code of 1986, as that section may be amended or renumbered;

Unless TRD can determine differently, it is assumed that energy storage systems are considered 15-year MACRS property and would be considered construction for which the explicit gross receipts tax, and companion compensating tax and local option compensating taxes in this bill would apply and create a revenue loss.

Similarly, Section 7-36-29 NMSA 1978 provides the general rule for the treatment of tangible personal property for the purpose of the property tax. The rule established in that section that if the asset is considered tangible personal property, then assessed value for property tax purposes

is the cost basis and straight-line depreciation for the life of the asset applied. The salvage value per statute is set at 20 percent.

EMNRD observes a technical issue in the provisions of this bill:

> "The definition of "energy storage equipment" in the bill is narrow, referring to the storage of electricity only produced by wind and solar generation. This definition may be unintentionally limiting in two ways."
>
> 1. "It is technically impossible to limit grid-tied energy storage to electrons produced only by wind and solar, as electrons on the grid move freely without any limitations (or identification of where they came from). As draft, the definition may limit the applicability of the industrial revenue bond to non-grid-tied (isolated) energy storage projects."
> 2. "Renewable energy generation does not only include wind and solar, but also might refer to geothermal, clean hydrogen, and/or other technologies not yet available. Limiting this definition to wind and solar generation only may be unnecessarily prescriptive in defining what constitutes 'renewable generation' within the state."
>
> "Unless the bill sponsors specifically intended to limit energy storage equipment to that which is co-located with wind or solar generation the definition as currently constructed is unnecessarily limiting. If the intention is to limit it to co-located facilities, it should be stated more explicitly. Please see EMNRD's suggested amendment below."

OTHER SUBSTANTIVE ISSUES

Several elements of this proposal should be discussed:

(1) This proposal may fail the "but for" test. That is, would renewable energy storage be constructed in the absence of these tax incentives or would the incentive be required to have renewable energy storage installed.

(2) These tax benefits will be exported, primarily to consumers in California, since the bulk of the produced power, supported by the energy storage facilities, will be sold to California utilities. If power can be sold more cheaply because of reduced tax liability, then that cost reduction will show up on California consumer's bills.

(3) The property tax valuation rules for electrical generation, transmission and distribution (Section 7-36-29 NMSA 1978) were developed in a strongly regulated environment. Any property taxes were automatically allowed when the investor-owned utilities proposed rate cases. In an increasingly unregulated environment, the property taxes and gross receipts taxes on construction are no longer automatically included in the price that unregulated producers can charge customers. The IRB treatment of renewable energy generation and storage by unregulated entities may level the costs to the producer, including property taxes over time and allow the producer to accurately engage in long-term contracts.

(4) For most projects involving economic development tax incentives, such as Tax Increment for Development Districts or Local Economic Development Act (LEDA), a sponsoring government is expecting short-term construction phase gross receipts tax, short term construction jobs and long term operating and maintenance jobs. It is uncertain whether a gross receipts tax deduction and no meaningful long-term jobs will mean that fewer county or municipal governments would be willing to negotiate an IRB pursuant to the provisions of this bill.

SUGGESTED AMENDMENTS

EMNRD suggests making the following edits to the definition of "energy storage equipment" in the bill to address the technical issue identified above:

> ". . . equipment that is installed for the purpose of storing **and providing** electric energy received from ~~a~~ ~~wind or solar~~ **the electric power grid** or **a co-located zero-carbon** electric generation facility, that uses mechanical, chemical, thermal, kinetic or other processes to store energy for release at a later time and related equipment."

The gross receipts tax deduction of section 3 should be separately reported to TRD so that the annual Tax Expenditure report can accurately report the foregone tax cost. There is no particular amendment that will easily allow reporting of the property tax abatements.

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL

Energy storage projects will not be eligible for industrial revenue bond funding and governments installing energy storage equipment will not receive gross receipts deductions for the purchase of such equipment.

POSSIBLE QUESTIONS

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

LFC Tax Expenditure Policy Principle	Met?	Comments
Vetted	✓	The provisions of this bill have been offered and debated in previous sessions.
Targeted		The unstated purpose of this bill is to assist in moving the state to a zero-carbon energy posture by mid-century. However, there is no clearly stated purpose, long-term goals or measurable targets.
Clearly stated purpose	✗	
Long-term goals	✗	
Measurable targets	✗	
Transparent	✓	
Accountable		The fiscal implications of these tax expenditures depend on uptake and are, therefore, indeterminate.
Public analysis	✗	
Expiration date	✗	
Effective		
Fulfills stated purpose	✗	
Passes "but for" test	✗	
Efficient	✗	At this point in the state's energy plan, money spent of a mix of wind, solar and, perhaps, nuclear energy would be more efficient than money devoted to minimal storage strategies.
Key: ✓ Met ✗ Not Met ? Unclear		

LG/al