FISCAL IMPACT REPORT

		LAST UPDATED	
SPONSOR	STBTC	**ORIGINAL DATE**	2/7/24
SHORT TITLE	Electric Generation Tax Sunset	**BILL NUMBER**	CS/Senate Bill 282/STBTCS
		ANALYST	Graeser

REVENUE*
(dollars in thousands)

Type	FY24	FY25	FY26	FY27	FY28	Recurring or Nonrecurring	Fund Affected
CIT		Indeterminate but minimal loss	($500.0) to (~$5,000.0)	($500.0) to (~$5,000.0)	($500.0) to (~$10,000.0)	Recurring	General Fund

Parentheses ( ) indicate revenue decreases.
*Amounts reflect most recent analysis of this legislation.
The symbol "~" implies an estimate of order of magnitude or approximation. See discussion by TRD and LFC in the fiscal implications section.

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT*
(dollars in thousands)

Agency/Program	FY24	FY25	FY26	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
TRD	Indeterminate but minimal	Indeterminate but minimal	Indeterminate but minimal		Recurring	General Fund

Parentheses ( ) indicate expenditure decreases.
*Amounts reflect most recent analysis of this legislation.

Conflicts with HB216, relates to HB252, companion to SB119, duplicates HB118.

Sources of Information

LFC Files

Agency Analysis Received From
Public Regulation Commission (PRC) on HB118
Energy, Minerals and Natural Resources Department (EMNRD) on HB118
Taxation and Revenue Department (TRD) on HB118

SUMMARY

Synopsis of STBTC Substitute for Senate Bill 282

The Senate Tax, Business and Transportation Committee substitute for Senate Bill 282 (CS/SB282/STBTC) removes an automatic expiration date (sunset) in Section 7-4-10-E(3) NMSA 1978 that permits certain electrical energy generators to use a single sales factor in calculating the amount of corporate income tax. Advantaged producers are those that do not require a certificate of convenience and necessity from the Public Regulation Commission. This category of electrical generation includes all the independent power producers, including Pattern Energy's Sun Zia project and other wind and other utility scale solar projects in the state.

This bill does not contain an effective date and, as a result, would go into effect 90 days after the Legislature adjourns, or May 15, 2024, if enacted. The sunset date repealed in this bill is for taxable years ending with the 2023 tax year.

FISCAL IMPLICATIONS

This bill expands a tax expenditure, a provision that reduces tax revenue by creating an exception, by removing a sunset date for applicability of the single sales factor method of apportioning corporate income tax. The cost is difficult to determine but likely significant, in the range of double-digit millions. LFC has serious concerns about the substantial risk to state revenues from tax expenditures and the increase in revenue volatility from erosion of the revenue base.

The provisions of the bill would affect all independent power producers, including Pattern Energy which recently announced plans to bring 3.5 gigawatts of wind energy to market by 2026. The cost of this one project, including the SunZia transmission line, will be an announced $10 billion[1]. With over 200 miles of the 550 miles of the transmission line in New Mexico, the property factor of the project in the three-factor corporate income tax apportionment factor would initially contribute about 0.55/3 in the formula. The sales factor would contribute nothing because none of the generated power would be sold in New Mexico. The payroll factor is largely unknown but would be minimal after construction was complete. For argument, assume that the payroll factor would be equivalent to the property factor. Overall, with the three-factor formula, the apportionment factor would be in the range of 0.37. This 0.37 would be applied to the federal taxable income for the entire company. With the provisions of this bill, the single factor would be zero because the project would have zero sales in New Mexico. The unknown is the profitability of the project over the years. The estimated impact in the table is shown as (~$5,000.0) or (~$10,000.0) based on planned expansions or installations already announced.

TRD has provided more extensive analysis, but with a substantially different table amount:

Estimated Revenue Impact*					R or NR**	Fund(s) Affected
FY24	FY25	FY26	FY27	FY28		
--	(Less than $500)	(Less than $500)	(Less than $500)	(Less than $500)	R	General Fund

> In the last three years, as reported in the 2023 New Mexico Tax Expenditure Report, approximately 37 taxpayers have opted to use the manufacturing single sales factor for apportionment, resulting in an average annual revenue reduction of $43 million. Among these taxpayers, a small fraction comprises electricity-generating facilities. The potential revenue increase that would have occurred with the sunset on January 1, 2024, is currently not factored into the December 2023 Consensus Revenue Estimating Group (CREG) forecast. Therefore, while the fiscal impact notes a loss in general fund revenue,

[1] See story on page A-8 of January 23, 2024, *Santa Fe New Mexican*.

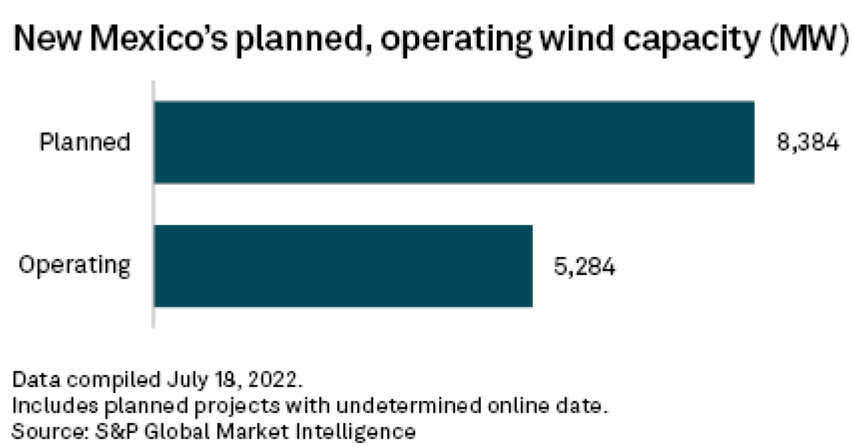
this loss is already considered in the CREG's December 2023 projections for FY25 through FY28.

With the completion of new electricity generation projects in the state, such as the Pattern Energy Western Spirit wind project, additional taxpayers are now eligible to make the apportionment election for manufacturers, specifically under the power generation category. The Western Spirit Wind project, finalized in 2021, encompasses four wind energy sites in Central New Mexico: Red Cloud, Duran Mesa, Clines Corners, and Tecolote, boasting a total installed capacity of 1,050 MW, or 1.05 GW.

Western Spirit Wind utilizes a total of 377 GE wind turbines ranging from 2.3 to 2.8 MW in capacity, supplying renewable energy to both California and New Mexico through long-term power purchase agreements. In California, these agreements involve the Los Angeles Department of Water and Power, San José Clean Energy, East Bay Community Energy, California Choice Energy Authority, and various member cities. In 2021, Pattern Energy entered into a 15-year power purchase agreement with Uniper SE for up to 219,000 MWh per year of wind energy. Uniper Global Commodities, an international energy company, plays a crucial role in providing power to New Mexicans.

As a result, a significant portion of electricity sales will take place in the large markets of California, providing substantial benefits to companies that choose to elect the manufacturing single sales factor for apportionment under the power generation category.

The chart below highlights the planned expansion of wind capacity in New Mexico.



At the current planned capacity of 8,384 megawatts (MW) in wind power—equivalent to 8.4 million kilowatts (KW)—and assuming full utilization each day, the monthly kilowatt hours1 (kWh) could potentially reach as high as 252 million. The average cost per kilowatt hour (cents/kWh) in New Mexico, spanning residential, commercial, and industrial sectors, is 9.73 cents/kWh[2]. While electric generation companies' average three-factor apportionment may not be significantly higher than the single sales factor, the potential revenue loss in Corporate Income Tax (CIT) revenue from wind generation alone may still be in the millions of dollars in the future as more companies establish in New Mexico.

SIGNIFICANT ISSUES

TRD discusses tax policy issues:

The Public Utility Act of New Mexico is a comprehensive set of laws that governs the regulation of public utilities in the state. It establishes the framework for the oversight, operation, and regulation of utilities that provide essential services such as electricity, natural gas, water, and telecommunications. The Act empowers the New Mexico Public Regulation Commission (NMPRC) to regulate and oversee public utilities to ensure that they operate in the best interest of the public. Electricity sold to New Mexico public utilities from generating stations is subject to this Act. The single sales factor election only applies to electricity generation at facilities that do not require NMPRC approval prior to commencing construction or operation' companies that are selling out-of-state do not require these approvals, and thus can elect the manufacturing single sales factor.

In general, corporations in New Mexico are required to apportion a share of their income to New Mexico for Corporate Income Tax purposes based on three factors. These three factors are the corporation's share of property, employment, and sales within New Mexico. Current law temporarily allows an exception to this three-factor apportionment formula for certain corporations receiving income from electricity generation facilities. Instead, those taxpayers are allowed to apportion income to New Mexico based only on their sales, and not on their property or employment.

The single sales factor apportionment is an incentive for multi-state firms the majority of whose sales are outside New Mexico. For qualifying domestic New Mexico companies, the single sales factor will reduce their income tax liability to the extent they have sales outside New Mexico. The purpose for having a single sales factor formula election for manufacturers is to encourage investment and employment in this state by manufacturers who do not anticipate substantial sales revenue within this state. Removing the sunset on the provision for electric generation taxpayers to elect the single sales factor supports future electric generation investment in particular renewable and sustainable electrical generation in the state as the majority of this generation will be sold outside of the state.

The removal of the sunset will maintain the erosion of horizontal equity among corporate tax filers who though equal in all other respects, i.e., taxable income, payroll, property and sales factors, are not eligible to elect the single sales factor.

EMNRD explains:

CS/SB282/STBTC removes a sunset date in the section of the tax code dealing with apportionment of business income, specifically in 7-4-10-E(3) NMSA 1978, to allow for the definition of "manufacturing" to permanently include power generation operations that do not require location approval and a certificate of convenience and necessity (CCN) from the Public Regulation Commission (PRC) to commence construction. As "manufacturing" businesses are exempt from the provisions in 7-4-10 NMSA 1978, this bill would enable those qualifying power generation facilities to elect single sales factor apportionment permanently.

The statute in question in CS/SB282/STBTC relates to corporate taxation, specifically whether a corporation is allowed to select single-sales-factor apportionment when paying state taxes or whether they are subject to three-factor apportionment like all other corporations. The statute specifies that manufacturers can select single sales factor apportionment, but not other types of businesses, unless they are headquartered in New Mexico. Single sales factor apportionment usually results in a lower tax rate for the corporation.

Under the statute as it stands, electric power generation is not considered a manufacturing business and must use three-factor apportionment, *unless* the electric power generation business does not require location approval and a CCN from the PRC to commence construction – but that exception expires in the 2024 tax year.

The exception provides a financial benefit to independent power producers (IPPs), who usually[2] do not need to apply to the PRC for location approval and a CCN, as they are presently allowed to elect single sales factor apportionment if they wish to. Most IPPs that operate in New Mexico are renewable energy companies. IPPs own 95 percent of extant wind and solar generation in New Mexico, and 94 percent of power generation owned by IPPs in the state is in fact wind and solar.

However, while three-factor corporate taxation is a burden on the corporation, it is more equitable for the state. Three-factor apportionment is calculated by taking the New Mexico-based percentage of a corporation's payroll, property, and sales, adding those together, and dividing by three to get the percentage of the corporation's net profit taxable in New Mexico. This means that the corporation is taxed in a way that reflects the 'benefit principle' – the benefits the corporation receives from the state, i.e., infrastructure, education, the legal system, police and fire protection, etc. Single sales factor apportionment taxes a corporation using a rate calculated only from the percentage of their sales which take place in New Mexico, ignoring payroll and land ownership (and thus the 'benefit principle').

Understanding the impact of the calculation requires an understanding of the assets a renewable energy-focused IPP tends to own in New Mexico. New Mexico is a secondary energy market for most national IPPs. Most of their sales by percentage are to other states such as California. What IPPs tend to own in New Mexico is land acreage, particularly for wind farm facilities. The percentage of their overall land portfolio which is in New Mexico is much higher than the percentage of their overall sales. Thus, three-factor apportionment will raise their corporate tax rates substantially and will make New Mexico a less attractive market for renewable energy companies.

> Pattern Energy recently broke ground on SunZia Wind and Transmission, a huge, 3.5-gigawatt wind farm that will send power from New Mexico to California via a 550-mile transmission line. The developer says it will be the largest wind development in the Western Hemisphere when it comes online in 2026 — generating about three times more power annually than the Hoover Dam.
> The project is vital to California's climate goals and is expected to deliver a surge of clean power to the state during the evening, when wind speeds accelerate, solar generation plunges and natural gas generation soars. SunZia is one of two massive wind projects that will serve California's hungry energy market. Chokecherry and Sierra Madre, a 3.5-GW wind project in Wyoming that will be served by a 732-mile transmission line, is expected to come online in 2029.
> Source: https://www.eenews.net/articles/biggest-us-wind-project-is-under-construction-in-new-mexico/

[2] https://closup.umich.edu/research/working-papers/utility-scale-renewable-energy-policy-landscape-new-mexico

The exception and its sunset were amended into Section 7-4-10 NMSA 1978 in the 2020 legislative session. Neither the apparent intent of the Legislature nor the policy of the governor's administration—which supports the development of a strong renewable energy industry in New Mexico—has changed in the intervening four years.

PERFORMANCE IMPLICATIONS

The LFC tax policy of accountability may be met because TRD recognizes the single sales factor apportionment as a tax expenditure and will report the impact in the annual Tax Expenditure Report. Subdetail, however, such as the headquarters cost or the cost of this manufacturing addition will not be reported because of redactions.

ADMINISTRATIVE IMPLICATIONS

The provisions of this bill will have minimal impact on TRD or EMNRD and no impact on PRC.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

Conflicts with:

HB216 which provides for a flat corporate income tax and requires all corporate income to be apportioned using a single sales factor.

CS/HB252/HTRC, the House Tax Package, also includes the HB216 provision on apportionment.

Companion to:

SB119, which provides for a flat corporate income tax rate.

OTHER SUBSTANTIVE ISSUES

In assessing all tax legislation, LFC staff considers whether the proposal is aligned with committee-adopted tax policy principles. Those five principles:

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

In addition, staff reviews whether the bill meets principles specific to tax expenditures. Those policies and how this bill addresses those issues:

Tax Expenditure Policy Principle	Met?	Comments
Vetted: The proposed new or expanded tax expenditure was vetted through interim legislative committees, such as LFC and the Revenue Stabilization and Tax Policy Committee, to review fiscal, legal, and general policy parameters.	✓	While the sunset repeal has not been discussed, the initial amendment was approved in 2020.
Targeted: The tax expenditure has a clearly stated purpose, long-term goals, and measurable annual targets designed to mark progress toward the goals. Clearly stated purpose Long-term goals Measurable targets	 ? ? ?	Allowing the single sales factor apportionment supports the state's renewable energy goals. However, most of the benefits of the provisions of the bill will go to producers selling power out-of-state.
Transparent: The tax expenditure requires at least annual reporting by the recipients, the Taxation and Revenue Department, and other relevant agencies	✗	CIT data for individual taxpayers would be redacted by TRD. There is no requirement for TRD to include single sales apportionment election in the annual TER.
Accountable: The required reporting allows for analysis by members of the public to determine progress toward annual targets and determination of effectiveness and efficiency. The tax expenditure is set to expire unless legislative action is taken to review the tax expenditure and extend the expiration date. Public analysis Expiration date	 ✗	The provisions of this bill remove a sunset.
Effective: The tax expenditure fulfills the stated purpose. If the tax expenditure is designed to alter behavior – for example, economic development incentives intended to increase economic growth – there are indicators the recipients would not have performed the desired actions "but for" the existence of the tax expenditure. Fulfills stated purpose Passes "but for" test	 ? ?	
Efficient: The tax expenditure is the most cost-effective way to achieve the desired results.	?	
Key: ✓ Met ✗ Not Met ? Unclear		

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