MINUTES
of the
SEVENTH MEETING IN 2010
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE
December 15, 2010
Room 307, State Capitol
Santa Fe

The seventh meeting of the Revenue Stabilization and Tax Policy Committee (RSTP) for 2010 was called to order by Representative Edward C. Sandoval, chair, on Wednesday, December 15, 2010, at 9:34 a.m. in Room 307 of the State Capitol in Santa Fe.

Present
Rep. Edward C. Sandoval, Chair
Sen. John Arthur Smith, Vice Chair
Sen. Carlos R. Cisneros
Rep. Nathan P. Cote
Rep. Anna M. Crook
Sen. Dianna J. Duran
Rep. Keith J. Gardner
Sen. Timothy Z. Jennings, Senate President Pro Tempore
Sen. Timothy M. Keller
Sen. Gay G. Kernan
Rep. Ben Lujan, Speaker of the House
Rep. Rodolpho "Rudy" S. Martinez
Sen. Howie C. Morales
Rep. Henry Kiki Saavedra
Rep. Thomas C. Taylor
Rep. Jim R. Trujillo

Absent
Sen. Tim Eichenberg
Sen. William E. Sharer

Designees
Sen. Mark Boitano
Sen. Phil A. Griego
Rep. Luciano "Lucky" Varela (attending as a guest)
Rep. Ray Begaye
Rep. Donald E. Bratton
Rep. Zachary J. Cook
Sen. Kent L. Cravens
Rep. Miguel P. Garcia
Rep. Roberto "Bobby" J. Gonzales
Sen. Clinton D. Harden, Jr.
Rep. Sandra D. Jeff
Sen. Carroll H. Leavell
Rep. Antonio "Moe" Maestas

Sen. Steven P. Neville
Rep. Debbie A. Rodella
Sen. Nancy Rodriguez
Sen. Bernadette M. Sanchez
Sen. John M. Sapien
Rep. James R.J. Strickler
Rep. Don L. Tripp
Sen. Peter Wirth

Other Guest Legislator Attending
Sen. Rod Adair

Staff
Pam Ray, Legislative Council Service (LCS)
Doris Faust, LCS
Ric Gaudet, LCS
Damian Lara, LCS

Minutes Approval

Because the committee will not meet again this year, the minutes for this meeting have not been officially approved by the committee.

Wednesday, December 15

Revenue Forecast

Secretary-Designate of Finance and Administration Dannette Burch, Secretary-Designate of Taxation and Revenue Duffy Rodriguez, Clinton Turner, chief economist, Taxation and Revenue Department (TRD), and Tom Clifford, chief economist, Legislative Finance Committee (LFC), presented to the committee the December consensus revenue estimate and economic outlook for New Mexico. Secretary-Designate Burch began by reporting to the committee that the new consensus revenue estimate has raised revenue projections by $56 million since the October estimate. This represents a 1.1 percent upward revision of the October estimate, which indicates that the bottom of the economic cycle has been realized and New Mexico is experiencing slow economic growth. Changes in the forecast are due largely to expected increases in gross receipts tax (GRT) revenue and federal mineral leasing revenue.

Secretary-Designate Burch said that the final audit for fiscal year 2010 would be issued soon and there would be no changes in revenue projections from the audit. Based on the Department of Finance and Administration's (DFA) final general fund report for fiscal year 2010, the department will transfer $172.6 million from reserve accounts to the general fund to close out the year. Fiscal year transfers to balance the books are estimated to total $39.6 million. The legislature authorized the administration to reduce general fund allotments to agencies if consensus revenue forecasts indicate a deficit will occur. The July 2010 revenue estimates resulted in allotment reductions of $150.9 million, and the October estimates indicated an additional $18.5 million shortfall. However, the December revenue estimates eliminated the need for any further fiscal year 2011 allotment reductions.

Mr. Turner reviewed the economic outlook for the state, which is projected to experience moderate growth in the next year. The GRT base is expected to grow 3.8 percent in the next year. With the inclusion of recent GRT rate increases, GRT revenues are expected to grow by 6.8 percent. Personal income tax (PIT) revenue for fiscal year 2010 is expected to be $957 million, which is more than $250 million lower than fiscal year 2008 levels. PIT revenue is expected to increase to $1.05 billion in fiscal year 2011 and increase slightly each subsequent year. Fiscal year 2008 levels will not be reached again until fiscal year 2015. Corporate income tax (CIT) revenue is expected to increase 76 percent in fiscal year 2011 to $220 million. CIT revenues are expected to increase more than 10 percent each year for the next several fiscal years.

Oil and gas tax revenues are estimated using price and production projections. The price of oil is expected to increase slightly each year. Oil volumes are also expected to increase in fiscal year 2011 but decline one percent per year afterward. Gas prices have remained below $4.00 per 1,000 cubic feet since September and are expected to increase only slightly due to large inventories in the national market. Although the dry gas price has remained low, New Mexico has benefitted from the premiums being paid for liquid gas products. Natural gas volumes in New Mexico have decreased 60 percent since 2008, and long-term predictions indicate that natural gas production will continue to slowly decline.

New Mexico's unemployment rate is currently at 8.8 percent. The Workforce Solutions Department expects the unemployment rate to slowly decrease over the next year, but that it will take several years before job creation eliminates the labor market slack created by the recession.

Mr. Clifford said that New Mexico is experiencing a very uneven economic recovery. Although overall gross domestic product (GDP) has increased, the retail and construction sectors are still in decline. National economic predictions have shown an overall growth rate of 2.5 percent in the next year. If the recently proposed tax incentive package Congress is considering is enacted, growth is expected to be three percent. Mr. Clifford said that New Mexico tax revenue would decline slightly from the tax cuts because the state uses the same income tax calculations that the federal government uses. Assuming a 4.4 percent revenue growth in fiscal year 2012, the deficit for the year, assuming the same level of services, will be $410 million.

Questions and comments from committee members included the following:

- The Tobacco Settlement Permanent Fund (TSPF) should not be considered a reserve for the general fund because money in that fund is not really available to be spent. If the TSPF is not considered a reserve fund, then operating reserves would actually be 2.7 percent and not the reported 4.5 percent.

- Do the projected increases in revenues from the rate increase of the cigarette tax take into account declines in smoking from the tax increase? Mr. Clifford said that the $.75 rate increase was predicated on tribes imposing the same $.75 tax on cigarettes. Tribes still have a $.91 differential with the rest of the state. Sales have not decreased very much since the tax rate increased.

- What would be the effect on CIT revenues from requiring multistate corporations to file combined tax returns? Mr. Clifford said that predicting the revenue impact of combined reporting legislation is difficult. He estimated a 10 percent to 15 percent increase in the CIT base from the change. However, corporations would be able to take other steps to minimize their long-term liabilities. Another idea would be to add back to a company's net income certain specific transactions that are considered to be purely tax avoidance schemes.

- Oil prices may actually rise above $100 per barrel, according to some estimates. Mr. Clifford said that oil prices have gone above $100 per barrel only once in history, during the recent economic bubble. It would not be wise to predict state revenues based on high oil prices.

- Dedicating five percent of the distribution from the Severance Tax Permanent Fund (STPF) for projects in colonias may be necessary, but those communities should also be required to provide some sort of in-kind contribution to the projects.

- The state relies on high cigarette taxes as a revenue source but then does not allow people to smoke in public places.

- State-funded capital outlay projects generate GRT revenue, which should be distributed to the state. Mr. Turner said that statewide, 56 percent of GRT revenues are distributed to the state.

- Infrastructure projects in colonias will allow economic development in those areas. Funding of those projects could be eventually phased out after basic infrastructure needs are met.

- Will capital outlay projects that get funded from a five percent distribution from the STPF on tribal lands generate GRT revenue for the state? Mr. Clifford said that most of those projects will still be part of the GRT base, except for projects that are performed completely by tribal entities. He said that many tribes have cooperative GRT revenue-sharing agreements with the state.

- Funding highway construction projects no longer creates the number of jobs that it used to because new highway construction technology requires fewer employees. Mr. Turner said that job training will be a critical component of the economic recovery. Former construction and manufacturing workers will not be getting jobs in the expanding health care sector without retraining.

- There has been discussion about dedicating funding for highway projects so that highways and bridges stay maintained and highway contractors would be able to keep their employees employed for the long term. Previous highway funding initiatives meant that there would be a large increase in employment, followed by a large decrease when the money ran out.

Natural-Gas-Propelled Vehicle Conversion Tax Credits

Speaker Lujan and Karin Foster, executive director, Independent Petroleum Association of New Mexico, presented a proposed bill to the committee to provide incentives for the purchase or conversion of vehicles that use natural gas instead of gasoline. The bill also encourages retail businesses selling gasoline to expand into dispensing natural gas for vehicle fuel. A PIT and CIT credits are proposed to provide for 70 percent of the cost, after any federal credit is applied, of converting motor vehicles to use natural gas. The PIT and CIT tax credits for expansion of a retail business to sell natural gas are for 50 percent of the cost. Finally, vehicles that are purchased new with natural gas as their power source will be exempt from the motor vehicle excise tax. The tax credits and exemption will end after five years.

Questions and comments from committee members included the following:

- How does a unit of gasoline compare to a unit of natural gas? Ms. Foster said that a gallon of compressed natural gas (CNG) has about the same performance as a gallon of gasoline. Currently, natural gas is selling at $1.00 less per gallon than gasoline. She said that the natural gas industry is willing to pay the current gasoline tax rate on sales of natural gas in order to ensure the solvency of the State Road Fund.

- What is the cost of conversion to natural gas? Ms. Foster said that a motor vehicle conversion costs about $12,000. It costs about $1.5 million to convert a gas station into a "fast-fill" natural gas station. Most fleet vehicles are currently refilled at less costly "slow-fill" facilities, but the refilling process takes several hours. The CNG industry needs retail infrastructure throughout the state in order for CNG-powered vehicles to become viable.

- Why is an incentive needed for vehicle conversions since people will be paying much less for fuel than for gasoline? Speaker Lujan said that this new technology needs to be supported at the beginning, in order to get people interested in using CNG in their vehicles.

Premium Tax Collection and Administration — Move to TRD

Ms. Ray presented legislation for the committee's consideration that would transfer the collection of the premium tax from the Public Regulation Commission (PRC) to the TRD. Ms. Ray said that the committee had previously expressed concern that the administration of the premium tax and related health insurance premium surtax was not being collected efficiently. The TRD may be a better entity to collect the taxes.

Questions and comments from committee members included the following:

- Is the TRD in favor of the legislation? Secretary-Designate Rodriguez said that the TRD has not yet considered the bill.

- Does the PRC collect any other taxes? Ms. Ray said that the Insurance Division of the

PRC does not collect any other taxes. It does, however, collect many different fees. David Lucero, analyst, LFC, said that the annual cost for administration of the premium tax is $420,000. The PRC has seven full-time employees that administer the system. The premium tax and surtax generate $200 million annually.

- How is the administration of the tax paid for? Mr. Lucero said that the PRC collects an administrative fee before revenue is distributed. Ms. Ray said that the current legislation does not provide for transfer of staff from the PRC to the TRD.

- The bill needs to be amended to include the transfer of surplus lines insurance premium tax collections.

The minutes of the November 29-30 meeting of the committee were adopted without changes.

Endorsements — Review of Proposals

The committee considered the endorsement of 14 proposed bills.

1) Repeal Venture Capital Investment Act. Ms. Ray said that this credit has never been used due to its complexity. The enactment of the angel investment credit has eliminated the need for the credit.

The committee endorsed the legislation unanimously.

2) Define "Modified Combined Tax Liability". Jim O'Neill, consultant and former TRD employee, said that the proposed bill fixes two technical issues in statute. When credits are allowed against various taxes, the question has arisen whether the calculation of distributions to local governments should reflect the credits taken. The TRD determined administratively 30 years ago that local governments should receive the full amount of the distribution without taking into account the credits. The proposed bill merely puts into statute what has been in practice for three decades. The bill also provides a uniform definition of "modified combined tax liability" for the various credits so that the TRD can administer the credits more efficiently. Taxpayers will not see any change from enactment of the bill, he said.

The committee endorsed the legislation, with Speaker Lujan voting against endorsement.

3) Confidentiality Exceptions for Tax Incentive Reporting. Ms. Ray said that this bill allows the TRD to disclose information about tax credits that otherwise would not be allowed. When a tax credit or incentive is claimed by only a few taxpayers, the TRD is not allowed to disclose any information about the cost of the credit because doing so would provide information about those individual taxpayers. The proposed bill would allow the TRD to disclose information it deems essential to assess the effectiveness of a tax incentive.

Committee members expressed concern that information about recipients of low-income tax benefits would be revealed by the TRD. Some members felt that the bill needs to be revised before it could be endorsed.

The committee voted to not endorse the bill, with Representatives Cote, Martinez and Saavedra and Senators Smith, Cisneros, Keller and Morales voting to endorse and Representatives Sandoval, Crook, Lujan, Taylor and Trujillo and Senators Griego, Kernan and Boitano voting not to endorse.

4) Itemized Reporting of Combined Reporting System (CRS) Deductions. Senator Keller said that in general, all deductions and exemptions from CRS taxes will be reported if the legislation is enacted. Most deductions currently are reported in the aggregate, which makes it difficult for the TRD to calculate the cost of each deduction. The bill will also require gross receipts to be reported for exempt transactions.

Committee members asked about the kinds of nonprofit organizations that will now be required to report their gross receipts. Ms. Ray said that most nonprofit entities that currently are exempt from the GRT will be required to report their gross receipts.

The committee adopted the legislation, as amended to delete new language that asserted the presumption that all nonprofit entities are subject to the GRT. Senator Kernan voted against endorsement.

5) Film Production Tax Credit Changes. Senator Keller said that the bill provides tracking requirements for film production companies claiming the credit; requires the posting of contact information for film production companies until all financial obligations in the state have been satisfied; requires an application for the credit to be made within one year of the company making final expenditures on a film; requires income tax to be withheld at the maximum statutory rate; requires a physical presence in New Mexico for expenditures to qualify for the credit; and requires the Economic Development Department (EDD) to provide an annual report on the credit's effectiveness.

Questions and comments from committee members included the following:

- The definition of "physical presence" is subject to interpretation by the New Mexico Film Division of the EDD. Lisa Strout, director, New Mexico Film Division, said that the place of business must be commensurate with the type of services being provided. Division staff will need to verify that a business qualifies as having a physical presence. Currently, some companies qualifying for the credit have a physical presence on paper only. This will mean additional responsibilities for the division, but the credit is intended to support New Mexico businesses.

- Will the new reporting requirements discourage the film industry from making films in the state? Ms. Strout said that the film industry is willing to comply with the additional reporting requirements.

- How will the film auditor hired by the State Investment Council (SIC) affect revenue to the state? Ms. Strout said that film audits are a standard procedure in the film industry. The state should be receiving revenue soon from investments it made through the SIC from several film productions.

The committee endorsed the legislation unanimously, as amended to correct a typographical error.

6) Tax Expenditure Budgeting. Senator Keller said that this bill is the same as a bill that was passed by the legislature in 2007 but was vetoed. It requires the TRD to compile a tax expenditure budget that lists the costs and benefits of all tax expenditures.

The committee endorsed the legislation unanimously.

7) Electric Plug-In Vehicle Tax Credit. Ms. Ray said that the bill exempts from the motor vehicle excise tax the purchase of new electric plug-in vehicles.

Committee members expressed concern that the exemption could apply to electric golf carts as well as the new cars being brought to the market.

The committee endorsed the legislation unanimously, as amended if necessary to clarify the golf cart issue.

8) Jet Fuel Deduction Extension. The bill would extend until 2017 the current 55 percent deduction from gross receipts and from computing the compensating tax of the sale of jet fuel.

The committee endorsed the legislation unanimously.

9) PIT Credit for Certain Out-of-State Employees. Ms. Ray said that the bill would provide a PIT credit of up to $1,000 for certain out-of-state employees of New Mexico logistics and distribution companies located in the border region of Santa Teresa.

The committee voted unanimously to not endorse the legislation.

10) Federal Low-Income Housing Credit Use in Property Valuation. Ms. Faust said that the bill is intended to end the divergent treatment by county assessors of property that has taken advantage of federal low-income housing credits to provide affordable housing. Some county assessors have added the value of the tax credit to the property assessment, which makes the development of these housing units no longer cost-effective.

Committee members expressed opposition to the bill and discussed that the real problem is that county assessors are not following the law in assessing properties. The bill is not needed because current law already mandates that county assessors take into consideration the decrease in value that would be realized by the owner in a sale of the property.

The committee voted unanimously to not endorse the legislation.

11) Above-Ground Storage Tank Installation Credit. Ms. Faust informed the committee that supporters of the legislation have withdrawn the bill from the committee's consideration. She said that the parties are pursuing a different resolution to the problem of complying with the state requirement of installing double-walled storage tanks by July 2011.

12) Natural-Gas-Propelled Vehicle Tax Credits. This bill had been presented to the committee earlier in the day. Speaker Lujan said that the fiscal impact from the legislation was estimated in the 2010 legislative session to be $3 million.

A committee member said that the credit for the installation of equipment to deliver CNG at retail stations is needed, but the vehicle conversion credit is probably not needed.

The committee endorsed the legislation unanimously.

13) Premium Tax Collection Change to TRD. This bill had been presented to the committee earlier in the day. Ms. Ray said that, after discussing the surplus lines premium tax with PRC staff, she believes that administration of that tax should not be switched to the TRD. PRC staff need to verify on a regular basis the tax, which is paid by out-of-state insurance companies.

Superintendent of Insurance John Franchini said that the premium tax and surtax generate $215 million annually for the state. The Insurance Division has four people who administer the tax. He said that the division is very efficient at collecting the tax and performing audits. Every time an insurance policy is written, the amount of tax due is reported to the PRC. PRC staff also audit every insurance company's financial statements to ensure compliance. The surplus lines premium tax is very complicated, and that insurance structure is currently being modified by the federal government. The administration of the premium tax does not need to be transferred to the TRD.

The committee voted unanimously to not endorse the legislation.

14) Provide for Review of Certain Tax Credits. Ms. Ray said that the bill provides for a periodic review by the committee of 28 tax credits. She said that the bill provides for review of the more commonly used economic development credits. She asked for input from the committee whether the review should be every four years or six years.

Questions and comments from committee members included the following:

- A four-year review period may send the message to businesses that the credit will be repealed, which may inhibit businesses to make investments in the state.

- Credits should have a specific date on which they expire, which still allows for a periodic review.

The committee endorsed the legislation unanimously.

There being no further business, the committee adjourned for the year at 3:04 p.m.