MINUTES
of the
SIXTH MEETING IN 2010
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE
November 29-30, 2010
Room 322, State Capitol
Santa Fe

The sixth meeting of the Revenue Stabilization and Tax Policy Committee (RSTP) for 2010 was called to order by Representative Edward C. Sandoval, chair, on Monday, November 29, 2010, at 9:18 a.m. in Room 322 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. Tim Eichenberg
Rep. Keith J. Gardner (11/29)
Sen. Timothy Z. Jennings, President Pro Tempore (11/29)
Sen. Timothy M. Keller
Sen. Gay G. Kernan
Rep. Ben Lujan, Speaker of the House (11/30)
Rep. Rodolpho "Rudy" S. Martinez
Sen. Howie C. Morales
Rep. Henry Kiki Saavedra
Rep. Thomas C. Taylor
Rep. Jim R. Trujillo

Absent
Sen. Dianna J. Duran
Sen. William E. Sharer

Designees
Rep. Miguel P. Garcia (attending as a guest 11/30)
Sen. Phil A. Griego (attending as a guest)
Sen. Clinton D. Harden, Jr.
Sen. Nancy Rodriguez (attending as a guest)
Rep. Luciano "Lucky" Varela (attending as a designee 11/29 and as a guest 11/30)

Rep. Ray Begaye
Sen. Mark Boitano
Rep. Donald E. Bratton
Rep. Zachary J. Cook
Sen. Kent L. Cravens
Rep. Roberto "Bobby" J. Gonzales
Rep. Sandra D. Jeff
Sen. Carroll H. Leavell
Rep. Antonio "Moe" Maestas
Sen. Steven P. Neville

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

Guest Legislator Attending
Sen. Cisco McSorley (11/29)

(Attendance dates are noted for those legislators not present for the entire meeting.)

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

Monday, November 29

Penalty Assessment Remittance — Agency Change

Patrick Simpson, deputy director, Administrative Office of the Courts (AOC), presented proposed legislation for the committee's consideration to change the process of administering traffic citations. The bill eliminates the requirement that motorists cited for a violation of traffic laws decide immediately whether to plead guilty or to contest the citation. Instead, motorists will have 30 days to either contest the citation or pay the fine. The bill also specifies that all fines and fees are to be paid to the AOC. Currently, uncontested citation fines and fees are paid to the Motor Vehicle Division (MVD) of the Taxation and Revenue Department (TRD), and contested citation fines and fees are paid to the AOC. The change will streamline the process of administering traffic citations, and it will relieve the MVD of those responsibilities. Magistrate and metropolitan court staff will see an increased workload from the change, so the bill creates a new traffic citation fee of $10.00, which will provide for additional staff at the courts. The MVD does not collect any money from the administration of traffic citations but funds the program through its general appropriation act budget. Mr. Simpson estimated that the magistrate courts will process 173,000 additional uncontested citations each year.

Questions and comments from committee members included the following.

- There are already too many fees that are added to a traffic citation. The proposed traffic citation fee is essentially a new tax that will fund government programs. Mr. Simpson said that the TRD supports the legislation, and it will reduce the workload of the MVD.

- The current structure of earmarking penalty assessment fees should be changed so that all fees are deposited into the general fund and the programs are funded yearly by the legislature.

- How will the revenue generated from the new fee be used? Mr. Simpson said that the money would be distributed to magistrate and metropolitan courts for the administration of traffic citations.

- The TRD budget should be reduced to account for its reduced workload if the legislation is enacted.

- Why does the bill give the AOC the ability to modify the uniform traffic citation form? Mr. Simpson said that the AOC wants to have more input into the citation form. Some changes made to the form in the past have not worked well for the AOC.

- How much money in fees is currently collected for a traffic citation from Section 35-6-1 NMSA 1978 versus Section 66-8-116.3 NMSA 1978? Mr. Simpson said that a person who is found guilty in contested cases, pursuant to Section 35-6-1 NMSA 1978, pays a total of $76.00 in the magistrate court and $80.00 in the metropolitan court. The total fees paid pursuant to Section 66-8-116.3 NMSA 1978 for uncontested citations is $61.00 in counties with a magistrate court and $55.00 in counties with a metropolitan court.

- The section in the proposed bill creating the traffic citation fund needs to specify that money in the fund can only be spent pursuant to legislative appropriation.

- Representatives of the MVD and magistrate courts should have appeared before the committee. Mr. Simpson said that the AOC represents magistrate courts. He said that the MVD is in favor of the change. The MVD currently has 20 full-time-equivalent (FTE) employees who administer all fees, fines and registrations included in the Motor Vehicle Code.

- This restructuring bill should have been presented to the Government Restructuring Task Force. Fern Goodman of the AOC said that the judiciary did present the idea of switching the administration of traffic citations from the MVD to the magistrate courts. However, the proposal was still in the development phase and was not in bill form.

- The $10.00 fee for each traffic citation will generate more money than needed for the magistrate courts. Where will the extra money be distributed? Mr. Simpson said that some magistrate courts will need additional personnel to manage the increased workload. Statewide, there may be a need for 10 to 20 additional FTEs, but the impact on the courts is still uncertain. Magistrate courts have already made large budget cuts in the past two fiscal years, and any more cuts will result in employee furloughs. While the proposed legislation will end up making the administration of traffic citations more efficient, magistrate courts will need additional revenue to implement the program. Money generated from the traffic citation fee will not be spent on AOC staff raises or other perks.

- The municipal penalty assessment program, commonly referred to as "red-light camera citations", that diverted money from magistrate courts to municipalities should be stopped. Traffic citations should not be a revenue source for municipalities.

Tourism Marketing Revenue Proposals

Secretary of Tourism Michael Cerletti and Deputy Secretary of Tourism Jennifer Hobson discussed with the committee several options for providing a dedicated revenue stream for the advertising program of the Tourism Department (TD). Secretary Cerletti began by reviewing the economic impact tourism has in New Mexico. Tourism spending in 2008 generated $6 billion in economic activity in the state and $765 million in federal, state and local tax receipts. The state realized $370 million in revenue from tourism in 2008, which accounts for about seven percent of general fund revenues. The department is underfunded; New Mexico ranks thirty-second in the nation in tourism advertising spending.

Ms. Hobson presented four options for providing a dedicated revenue stream for the TD.

- Redirect the $2.00 daily surcharge levied on rental car operations from the general fund to the TD budget. The $4.5 million generated by the surcharge each year would replace the $3 million general fund operating budget the department currently has.

- Dedicate 50 percent of any increase in Indian gaming revenue-sharing payments above fiscal year 2010 levels for the department.

- Enact a surtax of .25 percent of restaurant sales, which would be dedicated for TD advertising programs. The surtax would raise an estimated $6.5 million each year.

- Dedicate 3.5 percent of the average Severance Tax Permanent Fund yearly distributions, which would generate approximately $6.3 million each year.

Questions and comments from committee members included the following.

- The TD needs more advertising funding, but the money should be appropriated from the general fund rather than being earmarked from a particular source. Secretary Cerletti said that tourism is one of the top three industries in 49 states. Advertising funding has been cut 22 percent in the past few years, which has had a small negative impact on the number of tourists visiting New Mexico. Art Bouffard, president of the New Mexico Lodging Association, said that the past few years have been difficult for the lodging industry but occupancy rates are starting to increase. Martin Leger, advertising director, TD, said that several years ago, Colorado eliminated its tourism advertising budget and subsequently suffered tourism-generated revenue declines of 35 percent. He cited recent studies that found that for every $1.00 spent on tourism advertising, the state realizes $40.00 in economic activity.

- Does the state get any revenue from the occupancy tax? Secretary Cerletti said that all money generated by the tax is used by the local governments imposing the tax. He said the current structure of the tax is a good policy, and he recommended that distribution of its revenues not be changed.

- Has the New Mexico Restaurant Association (NMRA) endorsed the restaurant sales surtax idea? Allison Smith, government affairs director, NMRA, said that the association endorsed that idea in 2009 but has not considered endorsing the legislative proposal in 2010. The association is investigating other methods of raising tourism advertising revenues, she said.

- State money spent on public museums should be more fairly distributed around the state, which will increase tourism to those areas that currently receive no funding. Secretary Cerletti said that he expects that the opening of Spaceport America will be a tremendous boon to the tourism industry in the Las Cruces area. Ms. Hobson said that the TD has made an effort to advertise parts of the state besides the north-central region. She mentioned ecotourism promotions related to space tourism at the spaceport.

- When Colorado cut its tourism funding, rural areas and small businesses around the state suffered.

- How do New Mexico's occupancy tax rates compare to lodger's tax rates in the surrounding states? Mr. Bouffard said that the occupancy tax rate varies between three percent and seven percent, depending on the municipality. He said that if the total of the occupancy tax rate and the gross receipts tax (GRT) rate gets much higher than 13 percent, tourism revenues tend to decline in that area. Santa Fe's combined rate is above 15 percent, he said.

- Would the casino revenue-sharing agreements with tribes need to be amended in order to dedicate revenue toward tourism advertising? Mr. Leger said that the agreements only specify the amount tribes pay to the state, not how the state spends the money.

- Does New Mexico spend tourism advertising money promoting tribal casinos? Secretary Cerletti said that all TD advertising is generic. The presence of casinos is sometimes used as a method of attracting tourists, depending on the intended audience.

- Earmarking revenues is not a sustainable revenue source. The state needs to ensure that all entities pay some taxes, which will allow for more revenue for tourism advertising and other important state programs.

Tax Proposals

Senator Keller presented three proposed bills for the committee's consideration.

<u>Tax Expenditure Budgets</u>

This legislation would require the TRD to prepare annually a tax expenditure budget, tracking the costs and benefits of tax incentives and other credits, rebates, deductions and exemptions. The budget would include a projection of the costs of tax expenditures for all significant general fund revenue sources; the statutory basis for each expenditure; the amount of revenue the state forgoes for each expenditure; the beneficiaries of each expenditure, including the number of jobs created; and any significant unintended consequences of each expenditure. The proposed bill is nearly identical to the bill that passed both houses of the legislature almost unanimously in 2007 but was vetoed by the governor.

Questions and comments from committee members included the following.

- How would film production tax credit reporting have been different had this bill become law in 2007? Senator Keller said that much better information about the credit would have been available.

- What is the fiscal impact of the legislation? Senator Keller said that the 2007 fiscal impact report (FIR) estimated the tax expenditure budget would cost $100,000 annually. However, the TRD this year produced, in-house, a report that is essentially a tax expenditure budget, but for much less money.

- A tax expenditure budget will need to detail the tax expenditures granted to nonprofit entities, as well as to businesses. Senator Keller said that this legislation, coupled with another bill he is proposing to require specific reporting of all deductions and exemptions, will ensure that data be collected.

- The state needs to perform dynamic economic modeling of tax expenditures in order to measure the indirect impacts and forgone opportunities of those expenditures. Senator Keller agreed, but he said that kind of study is expensive. The legislation he is proposing requires reporting of many specific indicators but does not require dynamic studies.

- How will the number of jobs created be measured accurately? Senator Keller said that there is still a policy question of which state agency should develop the tax expenditure budget. The agency would use a standardized formula using existing methodologies to determine the number of jobs created.

- State agencies need the ability to share confidential information. Senator Keller said that a bill to allow sharing of confidential information was vetoed in 2009.

<u>Film Production Tax Credit Act</u>

The proposed bill would provide better tracking requirements for companies claiming the film production tax credit. Key provisions of the legislation include requirements for tracking the return on investment of the credit; the development of a standard form for reporting; the requirement that film production companies waive certain confidentiality provisions in order to receive the credit; providing for a five-year review and sunset of the legislation; and compiling existing statutes relating to the credit into a new "Film Production Tax Credit Act". Film production companies would be required to report the number of jobs created and total wages paid in New Mexico; the number of New Mexico residents employed; the total amount of GRT paid; and other information the TRD and the Economic Development Department determine to be necessary to evaluate the effectiveness of the credit.

Questions and comments from committee members included the following.

- Does the film production tax credit currently have sunset provisions? Senator Keller said the tax credit is permanent.

- The state provides no-interest loans to film production companies. Can a company get a loan from the state and qualify for the tax credit? Senator Keller said that there is nothing in statute prohibiting a company from receiving both incentives.

Itemization of GRT Deductions and Exemptions

The proposed legislation would direct the TRD to revise GRT and compensating tax forms to require taxpayers to itemize exemptions and deductions on those forms. Currently, the TRD cannot accurately quantify deductions and exemptions because they are not reported separately.

Questions and comments from committee members included the following.

- How will this legislation affect businesses? Senator Keller said that businesses already have to quantify each deduction they are claiming, but then they merely report the total of all deductions claimed. The new legislation will not cause any hardships because businesses are not required to do any more work, except to list the deductions individually.

- Senator Keller was asked to review the legislation with tax accountants for any potential problems before introducing the bill.

County and Municipal Right-of-Way Fees

The committee heard a presentation from a panel of county officials about the ability of counties to impose right-of-way (ROW) fees on public utilities for the use of those easements. Panel members included Tito Chavez, former state senator and consultant, New Mexico Association of Counties (NMAC); Harold Garcia, public works director, San Miguel County, and chair, NMAC Public Works Affiliate; Doug Moore, chair, Otero County Commission; Scott Krahling, commissioner, Dona Ana County Commission; Larry Moore, Quay County road supervisor and vice chair, NMAC Public Works Affiliate; Dan Bryant, county attorney, Otero County; Paul Gutierrez, executive director, NMAC; and Tasia Young, lobbyist, NMAC.

Mr. Garcia said that the NMAC Public Works Affiliate convened a ROW committee in order to address the problem created when the Public Regulation Commission (PRC) questioned the validity of existing ROW agreements between counties and utility companies. The PRC ruled that the agreements were not valid because they had not been reviewed by the commission. The decision of the PRC was appealed to the New Mexico Supreme Court, which overturned the PRC's decision. The ROW committee has been studying the issue of how to clearly establish statutory authority for counties to enter into ROW agreements with utility companies.

County roads are often damaged when utility companies access their infrastructure that is located under the roads. Some counties have entered into agreements with the companies as a means of offsetting the damage to county roads. Municipalities have clear statutory authority to enter into these agreements; however, a county's authority to do so is more vague.

Mr. Moore said that Otero County had been collecting ROW franchise fees since 1987, until recently when the PRC decided those agreements were not valid. Utility companies need to be charged for the damage they do to county roads; if not, then the county may be subsidizing utility companies, in possible violation of the anti-donation provisions of the Constitution of New Mexico. Mr. Krahling said that county officials want to formalize, in statute, the right of counties to enter into ROW agreements. Mr. Chavez said that the ROW committee has had three meetings with utility companies and municipalities, and the only remaining issue to resolve is how to establish fee structures for electric cooperatives and large industrial energy users. Mr. Bryant explained that the ROW committee is working on language to reflect the fact that many cooperatives do not use ROW easements on public roads, so they should not be subject to ROW fees.

Questions and comments from committee members included the following.

- Are counties trying to get the authority to grant new ROW easements? Mr. Bryant said that counties already have that authority; what they are seeking is the ability to recoup expenses from damage to county roads.

- Many county roads do not have written ROW easements; instead, counties often used prescriptive easements to make existing roads into county roads. Counties then granted ROW easements to utility companies through those roads, which may have violated the landowners' property rights. If a county cannot maintain a county road, it should deed the road back to the owner of the property. Mr. Moore said that county commissions have the legal authority over county roads. Otero County only gets $.05 per mile from the state, and it is charged with maintaining 1,600 miles of county roads. Utility companies often do shoddy work when accessing their infrastructure, leaving damaged roads as well as liabilities for the county if utility infrastructure is later damaged by road maintenance. He cited an example of a telephone company installing a high-speed phone cable only 14 inches below the ground. The following year, heavy rains washed out portions of the road, and a county road grader damaged the cable, for which the phone company demanded restitution.

- Instead of granting counties the authority to charge fees to utility companies, counties might need stronger enforcement capabilities to ensure that utilities meet quality standards.

- Can a county deny a utility access to its underground infrastructure? Mr. Bryant said that counties do not have the authority to deny ROW access to a utility company.

- Questions were raised about the locations of ROW committee meetings and whether all interested parties were included in the discussions. Mr. Gutierrez said that the NMAC Public Works Affiliate has representatives from all counties. The ROW committee will propose the recommended legislation to the full NMAC board for its consideration. If the board approves the idea, then each county representative will present it to individual county commissions. He said that the legislation will include the option for counties to opt out of entering into ROW agreements.

- Could the ROW fee be based on the number of miles of road used by a utility company, rather than a percentage of revenue? Mr. Chavez said that idea could work, except that it would be challenging to determine actual mileage.

- If counties get a fee from utility companies for ROW access, landowners should also receive some of that revenue.

- Counties have the ability to assess road maintenance fees, yet they are reluctant to raise taxes. Mr. Moore said that utility companies need to pay for the damage they cause to public roads; it would not be fair to tax county residents in order to pay for that.

Unemployment Trust Fund Solvency — Issues and Options

Secretary of Workforce Solutions Ken Ortiz discussed with the committee the solvency of the Unemployment Insurance Trust Fund (UITF) account of the Unemployment Compensation Fund. The UITF, which provides unemployment compensation, is projected to become insolvent by August 2011 unless some action is taken. Proactive steps were taken in fiscal year 2010 to maintain the UITF's solvency, but the 500 percent increase in unemployment benefit claims in the past 30 months has meant that the UITF will soon be unable to cover unemployment liabilities. The legislature recently transferred $117 million to the UITF from another state government unemployment trust fund; decreased the average weekly compensation from 60 percent to 53.5 percent; and increased the employer contribution levels, beginning in January 2011.

Without congressional action to fund extended unemployment benefits, the UITF balance will fall below zero in August 2011, assuming the unemployment rate remains constant at 8.4 percent. The federal extended benefits were scheduled to expire the following day, November 30, 2010, which meant that federal unemployment compensation tiers 1-4 will no longer be available. After that date, total benefits for new claims will be reduced from 93 weeks to 46 weeks in New Mexico, and the state will begin paying 50 percent of extended benefits beyond the regular benefit period of 26 weeks. In the worst case scenario, UITF insolvency will result in a mandatory loan from the United States Department of Labor, the automatic changing of employer contributions from level 1 to level 6 and the loss of a federal tax credit for employees. The employer contribution change will result in an average payment per employee of $512 per year, which would be more than a 200 percent rate increase.

Secretary Ortiz presented potential cost savings and revenue enhancements that the legislature could consider. He said that the Workforce Solutions Department (WSD) is not advocating any particular change because those policy decisions need to be made by the next administration. New Mexico has several additional unemployment benefits that add $71 million annually to the cost of the program, including extended/high unemployment period benefits; full-time student benefits; dependent allowance benefits; part-time work allowances; alternate base period calculations; military spouse benefits; and domestic violence benefits. Revenue enhancement options include increasing the employer contribution rate schedule; increasing the rate for new employer contributions; imposing a short-term surcharge on employers; and increasing penalties for delinquent filers.

Questions and comments from committee members included the following.

- How do the part-time work benefits function? Secretary Ortiz said that the people who are receiving unemployment compensation benefits and subsequently start working part time receive reduced benefits, rather than having their benefits terminated.

- Can a person receiving retirement benefits also receive unemployment compensation benefits? Clyde DeMersseman, general counsel, WSD, said that current law allows unemployment compensation benefits to be paid, but those payments are reduced according to the pension amount. However, the WSD can only act on information provided to the department, and some claimants do not inform the department that they are receiving pensions or other income.

- A few years ago, the UITF had a huge surplus, so the legislature froze the employer contribution rate at schedule 0.

- How do extended-week benefits work? Secretary Ortiz said that basic benefits are for 26 weeks, fully paid for by the state. There are four tiers of federal benefit level extensions, which are triggered based on the state's unemployment level. Those federal extensions have been funded completely by the federal government, but the state will begin paying 50 percent of those benefits December 1, 2010, unless Congress authorizes more funding at the federal level.

- Unemployment compensation benefits should not be paid to people who fail a drug test. Mr. DeMersseman said that some states have attempted to implement that idea, but courts have ruled against that approach. An alternate possibility would be to condition benefits on "readiness to work", which could be defined as being drug-free.

- Will reductions in the additional benefits help the solvency of the fund? Secretary Ortiz said that the additional benefits, other than extended-week benefits, account for less than 10 percent of total annual expenditures from the fund. Cuts in those areas could help, but they have been identified as socially important or economically beneficial. The domestic violence benefit, while not being an economic development tool, only costs $162,000 and provides benefits to people who are forced to quit their jobs due to domestic violence issues.

- Would a college instructor who teaches two semesters of courses be eligible for benefits during the summer months? Mr. DeMersseman said that educational employees are treated differently from employees of most other industries. An individual's "attachment to the workforce" is considered before benefits are granted. Thus, a college instructor would have a reasonable expectation of being rehired and would not be eligible for benefits.

- Would military retirees who move to another state be eligible to collect unemployment compensation benefits? Mr. DeMersseman said that federal regulations for military retirees are different than for other industries. He will research that question and report back to the committee.

New Mexico Municipal League Legislative Priorities

Bill Fulginiti, executive director, New Mexico Municipal League (NMML), discussed with the committee the league's priorities for the upcoming legislative session. Rather than asking for legislation to be enacted, Mr. Fulginiti said the NMML is asking that the state not enact any legislation that would result in the loss of municipal revenues or any legislation that would preempt the ability of municipalities to tax certain transactions. He reminded the committee that, on average, 75 percent of all municipal revenues are derived from the GRT, and the recent economic recession has hurt municipalities. GRT revenue declines have ranged from one percent to 39 percent. The City of Belen has laid off 25 percent of its city employees and is still facing a $3.8 million shortfall. The City of Albuquerque has a $66 million deficit, which is about eight percent of the city's general fund budget.

If the legislature enacts a law to repeal the "hold-harmless" provisions in statute, designed to protect city revenues from the gross receipts deduction allowed on food, municipalities will be faced with an even greater budget shortfall. That change would result in a loss of revenues to Albuquerque of 8.8 percent, and to Hatch of 30 percent.

Questions and comments from committee members included the following.

- Has there been any congressional movement on the issue of taxing internet sales? Mr. Fulginiti said that, unfortunately, online companies have been essentially purchasing congressional members in order to stall that legislation.

- Albuquerque still has unused GRT taxing authority. Every entity in the state needs to share in the pain of budgetary shortfalls, and the hold-harmless provisions need to be revisited. Municipalities were the recipients of a revenue windfall a few years ago when fiscal projections of the GRT food deductions were incorrect. Mr. Fulginiti said that municipal GRT increases have to be approved by the voters, which is not always easy to do. When food was part of the GRT base, the revenues generated by the GRT had been pledged to the payment of revenue bonds. The hold-harmless provisions ensured the bonds' repayment, which had been guaranteed by the state in statute. If the state removes the protection of those bonds, bond-rating agencies will reduce the state's bond ratings, which will cost state and local governments far more money than the hold-harmless provisions currently do.

- Will cities benefit if the GRT is reimposed on food? Mr. Fulginiti said that the legislature passed in 2010 a bill to have a local option GRT on food, which legislation would be acceptable to municipalities. The governor repealed that legislation, however.

- Taxing food purchases of low-income people is a regressive tax policy, but most middle- and high-income people should pay the GRT on food.

● How did the vetoed distribution of cigarette tax revenues to municipalities happen? Mr. Fulginiti said that when the cigarette tax rate was raised in 2010, the distribution of the tax to various existing recipients was also changed to reflect the tax rate change. Although the distribution to municipalities had been in statute for years and was not being substantively modified, the governor deleted the entire distribution from the act. Mr. Fulginiti said that municipalities were very surprised at the line-item veto.

Electric Car Tax Credit

Representative Trujillo and Murray Thompson, lobbyist, General Motors (GM), presented a proposed bill that would grant a one-time exemption from the motor vehicle excise tax from the sale of qualified electric plug-in electric drive vehicles. The tax credit would be available from 2011 to 2014. Mr. Thompson said that the Chevrolet Volt, which is expected to be on the market in 2011, is the first of the next generation of alternative energy vehicles. A fiscal impact report has not yet been prepared for the legislation, but last year, it was estimated that it would cost $1.5 million annually. GM will manufacture 10,000 of these cars in 2011, and 30,000 in 2012.

Questions and comments from committee members included the following.

● How much will the Volt cost? Mr. Murray said the base price for the car is $41,000. It has a top speed of 100 miles per hour.

● Inversely indexing the amount of the tax credit to the price of gasoline would have the effect of stimulating car sales through tax incentives when gas prices are low, but when gas prices are high, natural market forces will have the same sales effect without the need for this credit.

The committee recessed at 5:30 p.m.

<u>Tuesday, November 30</u>

The committee was reconvened at 9:17 a.m. on Tuesday, November 30, 2010, by Representative Sandoval.

City of Las Cruces and Mesa del Sol Tax Increment Development District Updates

Senator Mary Kay Papen; Larry Horan, lobbyist, City of Las Cruces; Mike Daly, president, Mesa del Sol; and Tom Horan, lobbyist, Mesa del Sol, gave an update of two tax increment development districts (TIDDs) in the state. Senator Papen sponsored legislation authorizing the City of Las Cruces Main Street Downtown TIDD to receive the state portion of GRT revenues realized from extra economic activity in the TIDD. She said that the Las Cruces TIDD will be beneficial to the city and will create jobs in the area. Larry Horan said that the TIDD has just received the first increment from the state, which has amounted to $1.8 million. Most of the economic activity from the district has been from the reconstruction of Main Street and from work on the Rio Grande Theater. He estimated a net gain of 200 jobs from the projects. The city has completed construction of a new city hall and is currently looking for tenants for the old building. Private development is beginning to occur in the area, and the farmers' market has brought many residents downtown to shop.

Mr. Daly updated the committee on the Mesa del Sol TIDD, which was created in 2006. The legislature in 2007 authorized up to $500 million in bonding capacity over 25 years from economic activity in the district. Mesa del Sol receives tax increment dedications from the state, the City of Albuquerque and Bernalillo County. The first bonds were issued in October 2009, with $3.6 million being reimbursed for public infrastructure. Current commercial tenants include Albuquerque Studios, Fidelity Investments, Schott Solar, Molina Healthcare, MSR-Fraunhofer, the Aperture Center and the federal Drug Enforcement Agency and Immigration and Customs Enforcement. Mesa del Sol has built a school for an international baccalaureate charter elementary school, which is the first of its kind in the state. All of the green space areas of the development used locally grown plants, and recruitment programs in the South Valley of Albuquerque have resulted in 25 people being hired by Mesa del Sol's businesses. Finally, Mr. Daly said that his company has invested $80 million into Mesa del Sol, and it is here to stay. The company has not earned a profit yet, but he expects that milestone will be passed in the near future.

Questions and comments from committee members included the following.

- How much does land cost in the development? Mr. Daly said that Mesa del Sol started selling land at $2.50 per square foot but needs to reach $5.00 per square foot in order to become profitable. He compared the price of land at Mesa del Sol to other developments with much higher land prices.

- When will residential development begin? Mr. Daly said that he expects construction to begin in 18 months. He said that he believes the residential real estate market will not recover until 2014.

- Does Mesa del Sol provide state office space for free? Mr. Daly said that staff for the state's supercomputer has been provided free space until the building finds a commercial tenant.

- What is the status of potential new interchanges on Interstate 25? Mr. Daly said that $20 million in state funding and $2 million in Mesa del Sol funding have been allocated for a new interchange.

- The charter school will be open to all Albuquerque Public Schools (APS) students, so transportation could be an issue. Additionally, residents of Mesa del Sol will not have any enrollment preference. Mr. Daly said that the law requires that charter schools be open to all students in a district. There will eventually be a regular public school in the area, but until then, Mesa del Sol has agreed to pay APS $3,000 in impact fees for every student in the development attending an APS school.

- Mesa del Sol has done a great job of economic development. The news media have unfairly portrayed TIDDs as draining resources from developed areas to new developments.

Necessary Tax Deductions and Exemptions Distinguished from Tax Expenditures

Tom Clifford, chief economist, LFC, discussed tax expenditures in statute and how they could be evaluated. He began by reviewing the LFC's adopted good tax policy principles of adequacy, efficiency, equity, simplicity and accountability, and he mentioned that targeted expenditures like tax incentives necessarily conflict with the simplicity principle. Tax expenditures, broadly defined, are revenue losses from tax provisions that grant special relief designed to encourage certain kinds of behavior or to aid taxpayers in special circumstances. Advantages of using tax expenditures to affect policy include the ability of using an existing government system to target expenditures and the relative ease of gathering information to be able to accurately target the expenditure. Disadvantages include their inherent inequity, complexity and lack of transparency and the lack of control by policymakers over their budgetary impacts.

Mr. Clifford categorized 96 tax expenditures found in New Mexico statutes. Economic development incentives will cost the state $104.6 million in fiscal year 2012 general fund revenues; anti-poverty, health and education incentives will cost $367.5 million; renewable energy incentives will cost $24.5 million; and other incentives will cost $444.5 million.

Economic development incentives include the film production tax credit, which is estimated to cost $70 million this year; the investment credit, costing $7 million; the technology jobs tax credit, costing $6.6 million; and the high-wage jobs tax credit, costing $5.6 million. Economic development incentives provide targeted relief to encourage businesses to start up in or relocate to New Mexico and may cover up other deficiencies the state may have in attracting businesses. However, many of these incentives lack accountability and reporting requirements, and the complexity of some incentives may actually undermine their effectiveness.

Health care expenditures cost the state $220 million and mostly consist of the insurance premium tax credit for $77 million, the GRT deduction from managed care services for $75 million, the GRT prescription drug deduction for $19 million and hospital credits and deductions for $23.5 million. Although health care tax credits may be intended to improve health care delivery in the state, the uneven treatment of the credits is not fair to large segments of the population. Since one-third of the state's revenues is spent on the health care sector, exempting large portions of that industry from taxation may compromise the adequacy of state revenues.

Anti-poverty incentives include the working families tax credit, which will cost $45 million; the exemptions from income taxation of low- and middle-income households, which cost $30 million; the low-income comprehensive tax rebate, which costs $24 million; and the federally mandated exemption from the GRT on food stamps, which costs $20 million. Although targeting of relief can easily be achieved through the tax system, some forms of targeting may not actually benefit the intended recipient. Administrative costs may also outweigh some of the benefits. Mr. Clifford said that although the overall tax system in New

Mexico is regressive, state spending is progressive.

Renewable energy incentives include various energy production credits, costing $20 million, and a GRT deduction for wind energy equipment, costing $2 million. Issues with renewable energy incentives include that the tax system is an inefficient system to administer these complex incentives; the public benefits of renewable energy are not quantifiable; the layering of various incentives means that large subsidies are being offered to the industry; and sunsetting provisions will be needed to prevent erosion of the tax base if the industry grows larger.

Other tax expenditures include the deduction of food receipts from the GRT, which will cost $217 million; the cigarette tax exemption for tribes, costing $75 million; the oil and gas emergency school tax royalty deduction, costing $40 million; the deduction from income tax of capital gains, costing $37 million; and certain insurance company receipts not being taxed at all, costing $26 million. Concerns with some of these expenditures include that some expenditures, like the food deduction, do not benefit low-income households. The cumulative revenue impact of these tax expenditures also raises adequacy concerns.

Mr. Clifford then described "normal" exemptions and deductions, which, for various reasons, are necessary but would not be considered tax expenditures or incentives. Some exclusions are designed to prevent double taxation on items such as investment income, wages, dividends, motor vehicles, most oil and gas activities and fuel. Other exclusions are designed to prevent pyramiding of the GRT, including many business-to-business transactions, agricultural products, commissions, sales for resale and energy used in production activities. Other activities have been excluded from the tax base, including sales by governments, some sales of nonprofit entities, pass-through entity income exclusions and activities preempted by federal law from taxation.

Mr. Clifford then discussed various tax rate differentials, which could be considered tax expenditures or disincentives. While the average GRT rate in New Mexico is seven percent, other taxes that involve sales range between one percent and 30 percent. There are often mitigating reasons for the differentials, such as additional taxes paid by the industry, but the legislature should periodically study those issues to ensure that the tax system is equitable. Finally, Mr. Clifford discussed accountability provisions that should be considered, including tax expenditure reports that include detailed summaries of measurable indicators, independent audits of information, dynamic economic analyses of incentives and a determination of incentives' cost-effectiveness.

Questions and comments from committee members included the following.

- Why are some of the incentives so complex? Mr. Clifford said that some health care incentives have proven to be more complex than initially thought. There are many gray areas in types of medical services, and it is difficult to interpret criteria to qualify for an incentive. Many businesses have also expressed concern about the long amount of time it takes the TRD to approve some credits.

- How regressive is New Mexico's tax burden? Mr. Clifford said that the lowest-income households pay 10 percent of their incomes in taxes, compared to seven percent for middle-income households. State spending, however, is very progressive. Looking at tax burdens on businesses, New Mexico ranks average among states, if severance taxes are excluded from the calculation.

- If New Mexico broadened its tax base to ensure that everyone is taxed, could tax rates be lowered? Mr. Clifford said that policy is theoretically possible, but it would be easier when the state is not facing budget shortfalls. The GRT pyramiding problem is significant; studies indicate that the effective GRT paid is much higher than the statutory rate.

- Pyramiding is a problem, but the legislature continues to narrow the tax base and raise rates. Mr. Clifford said that the recent one-eighth percent increase in the GRT rate raised $50 million in revenues, compared to the $217 million lost from the narrowing of the base from the food deduction. The corporate income tax (CIT) also has a very narrow base, such that most businesses in the state do not pay the CIT.

- How can economists study the economic activity that would have occurred if the tax incentive were not in place? Mr. Clifford said that those studies are very complicated, but that they need to be performed periodically in order to evaluate the complete economic impact of an incentive. He said that even though a business relocation may appear to be beneficial to the state, the costs of the state's provision of government services to those businesses and employees need to be considered.

- The differential between the motor vehicle excise tax rate of three percent and the GRT rate has been discussed by policymakers for years.

- Mr. Clifford was asked to research the types of insurance transactions that are not taxed at all in New Mexico.

Cable Television Update

Susan Bitter Smith, executive director, and Scott Scanland, lobbyist, Arizona-New Mexico Cable Communications Association; Shirley Getz of Cable One; and Chris Dunkeson of Comcast updated the committee on the cable telecommunications industry in the state. Ms. Bitter Smith said that the association represents several smaller cable television providers in addition to Comcast and Cable One. The cable television industry is regulated by the Federal Communications Commission (FCC) and is also regulated and franchised by local communities. Franchise fees are paid to municipalities, and communities are able to design listings according to their own needs. The cable television industry is committed to providing broadband access to the entire state. Comcast has more than 200,000 subscribers and 505 employees in New Mexico. Its total tax liabilities and franchise fees amount to more than $8.6 million. Cable One has

25,000 subscribers and 60 employees in the state. It pays $750,000 in franchise fees, $200,000 in property taxes and $1.4 million in GRT each year.

Questions and comments from committee members included the following.

- Is the cable television industry regulated by the PRC? Ms. Bitter Smith said that the FCC is in charge of regulating the industry.

- To what extent do cable television companies in the state compete with the telephone company Qwest? Ms. Bitter Smith said that although the industries compete on some services, Qwest is a state-regulated utility that has a guaranteed rate of return for some services. Unlike Qwest and other phone companies, the cable television industry is entirely privately capitalized.

- Do cable television rate increases go through an approval process? Mr. Dunkeson said that some municipalities regulate rates, provided that authority is in their franchise agreement.

- Mr. Dunkeson was asked to provide the committee with a list of the amounts Comcast pays in franchise fees, property taxes and GRT.

- Some people feel that the provision of internet access is a function of a public utility and should be regulated by state utility commissions. Ms. Bitter Smith said that she believes the FCC will soon provide nationwide regulations in this arena. The cable television industry does not support state-by-state regulation of the provision of internet services.

The minutes of the October 25-26, 2010 meeting of the committee were adopted without changes.

Tax Incentive Discussion

Ms. Ray led the committee in a discussion about possible legislation for the committee's endorsement. Committee members decided to consider endorsement of legislation at its December meeting. Ms. Ray presented the following three proposed bills for the committee to consider.

- Repealing the Venture Capital Investment Act, which credit has never been used since its enactment in 1993. Staff was instructed to consult with a state venture capital association prior to the committee's endorsement.

- Making uniform the calculation of modified combined tax liability for tax credit purposes. There are currently many statutory tax credit provisions that allow a credit against multiple taxes, but all of these use slightly different definitions of which taxes can be used and of how liabilities are calculated.

- Allowing the TRD to share certain confidential taxpayer information with the legislature, which will allow the legislature to determine the effectiveness of tax incentives. Ms.

Ray said that the TRD has commented on the current version of the legislation. The TRD indicated that broad disclosure requirements could be a disincentive for businesses to engage in the targeted activity.

The committee discussed other legislation for consideration at the December meeting, including the sunsetting of all tax incentives; the periodic review of every tax exemption, credit and deduction; the capping of the total amount of some tax credits; the repeal of unused or ineffective tax incentives; the conversion of all exemptions to deductions or credits to ensure that they are reported; and the review of all earmarked revenue sources.

The committee, upon the recommendation of Speaker Lujan, decided that it may need to meet an additional day, on December 16, in addition to the December 15 meeting date.

There being no further business, the committee adjourned at 12:45 p.m.