MINUTES
of the
FIFTH MEETING IN 2010
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

October 25-26, 2010
Room 322, State Capitol
Santa Fe

The fifth meeting of the Revenue Stabilization and Tax Policy Committee (RSTP) for 2010 was called to order by Representative Edward C. Sandoval, chair, on Monday, October 25, 2010, at 9:20 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 (10/26)
Rep. Anna M. Crook
Sen. Tim Eichenberg
Rep. Keith J. Gardner
Sen. Timothy Z. Jennings
Sen. Timothy M. Keller
Sen. Gay G. Kernan (10/25)
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. Dianna J. Duran
Sen. William E. Sharer

Designees
Sen. Mark Boitano
Sen. Kent L. Cravens (10/26)
Sen. Phil A. Griego (attending as a guest)
Sen. Clinton D. Harden, Jr.
Rep. Debbie A. Rodella (attending as a designee 10/25 and as a guest 10/26)
Sen. Nancy Rodriguez (attending as a guest)

Rep. Ray Begaye
Rep. Donald E. Bratton
Rep. Zachary J. Cook
Rep. Miguel P. Garcia
Rep. Roberto "Bobby" J. Gonzales
Rep. Sandra D. Jeff
Sen. Carroll H. Leavell
Rep. Antonio "Moe" Maestas
Sen. Steven P. Neville
Sen. Bernadette M. Sanchez
Sen. John M. Sapien
Rep. James R.J. Strickler
Rep. Don L. Tripp

Rep. Luciano "Lucky" Varela
Sen. Peter Wirth

Other Legislators Attending
Rep. Ernest H. Chavez (10/26)
Sen. Cisco McSorley (10/25)

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

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

<u>Monday, October 25</u>

Tobacco Settlement Permanent Fund Receipts — Definition Change

Betsy Glenn, deputy attorney general, and Nan Erdman, assistant attorney general, presented a proposed definition change in cigarette tax statutes. Ms. Erdman said that a mistake was made during the last legislative session when cigarette taxes were raised. The result of that legislation is that some cigarette companies are no longer required to deposit a percentage of their cigarette sales on tribal lands into an escrow account. In 1999, New Mexico entered into the Master Settlement Agreement (MSA) with major tobacco companies that required companies to pay the state for every cigarette sold. Since then, more than 50 companies have joined the settlement. One of the conditions of the settlement was that New Mexico enact a statute requiring that nonparticipating companies contribute to an escrow account a percentage of their cigarette sales. This was needed in order to remove the competitive advantage that nonparticipating companies would otherwise have.

In 2010, the legislature raised the cigarette tax but provided for the same 91-cent differential between tribal and nontribal sales. By adding an additional category of cigarette tax stamp and stating that it was not an excise tax stamp pursuant to the Cigarette Tax Act in Chapter 7 NMSA 1978, confusion occurred over the definition of "units sold", a term used in the nonparticipating manufacturers' escrow statutes in Chapter 6 NMSA 1978. The question was whether the cigarettes sold by nonparticipating manufacturers were still considered to be stamped with "tax exempt" stamps. Tax-exempt stamped cigarettes are explicitly mentioned in the definitions of "units sold", thus allowing any cigarettes sold in a pack bearing a tax-exempt stamp to be counted toward the number of units sold in the state for purposes of determining escrow payments. The question has allowed nonparticipating manufacturers to argue that because some of their cigarettes are sold with tax-credit stamps, they are not tax-exempt stamps under the definition of "units sold" and are therefore not counted for purposes of payment of escrow. The Office of the Attorney General (AGO) wants to be certain that the escrow requirement is in statute. The office also wants to require that tobacco products sold by tribes be on the approved list of tobacco products, which will ensure that dangerous chemicals are not added to tobacco products sold in the state.

Ms. Erdman said that participating companies are alleging that New Mexico is not diligently enforcing the settlement. Nonparticipating companies are using tribal lands to import cigarettes without collecting the escrow amount. If the participating companies prevail in their case, New Mexico stands to lose annual tobacco settlement funds paid to be the state as well as escrow payments beginning July 1, 2010.

Questions and comments from committee members included the following:

• A committee member said that he had asked a representative of the AGO during the legislative session whether the cigarette-tax-raising proposal would have any effect on the MSA. The AGO representative had indicated that there were no problems with the legislation. Ms. Erdman said that the person who had testified before the legislature no longer works with the AGO. She said that she had not seen the legislation before it was voted on by the senate. The 2010 change in statute effectively undid the change made in 2009, which required that tribal sales by nonparticipating companies have the escrow requirement.

• How is the escrow amount collected? Ms. Erdman said that escrow money is not a payment to the state, but the money is set aside if the state decides to sue nonparticipating companies for the costs the state incurs as a result of cigarettes being sold. The cigarette taxes are paid to the state or tribes by the distributor of the cigarettes. MSA payments are made by cigarette manufacturers to the state. The average MSA contribution is about $5.30 per carton sold in the state.

• The AGO had plenty of time during and after the session to ensure that the language in the cigarette tax bill was adequate. For example, the bill was in the House Taxation and Revenue Committee for three days. The AGO staff should have done a better job.

• How are the tax-credit stamps created by the new legislation regulated, and how are illegal cigarette shipments stopped? Ms. Erdman said that a distributor receives a tax-credit stamp for tribal sales if the tribe imposes a tribal cigarette tax. Illegal shipment of cigarettes has been a big problem in the past. The AGO has managed to shut down some companies that were importing cigarettes illegally. The new legislation proposed by the AGO will address the illegal cigarette problem somewhat, and it will actually reduce the work load of the office.

• How much money is currently in the escrow account? Ms. Erdman said that there is approximately $72.8 million in the account. Interest in the account is returned to the manufacturers.

• Why has the state not sued the nonparticipating manufacturers? Ms. Erdman said that the AGO does not have enough resources to pursue that litigation.

Joe Thompson, a lobbyist representing Native Traders, a nonparticipating tobacco company, said that his company has a much different perspective on the AGO's legislation. He said that the escrow requirement change was not an oversight at all; rather, it was part of the deal that made the legislation acceptable to the parties. He said that the change proposed by the AGO would be a betrayal of the deal made with the tribes.

Revenue Forecast and Fiscal Update

Dorothy Rodriguez, secretary-designate of taxation and revenue, Dannette K. Burch, secretary-designate of finance and administration, and Tom Clifford, chief economist, Legislative Finance Committee (LFC), presented a revenue forecast and fiscal update to the committee. The forecast was developed by the Consensus Revenue Estimating Group, consisting of career economists at the Department of Finance and Administration (DFA), the Taxation and Revenue Department (TRD), the Department of Transportation (DOT) and the LFC. Secretaries-Designate Burch and Rodriguez presented the revenue estimate first.

Changes in the revenue estimate from July 2010 indicate that fiscal year 2011 revenues will decrease another $40 million and that projected revenues for fiscal year 2012 will decrease $81 million. Weaknesses in gross receipts and selective sales taxes were important factors in the downward revision of the fiscal year 2011 estimate. General fund reserves are expected to drop an additional $18.5 million from the July estimates, which leaves a 3.5 percent reserve level at the end of fiscal year 2011. The administration was granted authority to adjust budgetary allotments downward, but the administration does not currently propose such a move because agencies have already been preparing for a mid-fiscal-year reduction in their budgets of three to five percent.

The key economic indicators for New Mexico predict that the decelerating growth observed in the second and third quarters of 2010 will not likely result in a "double-dip" recession. Although the state's gross domestic product (GDP) grew by less than one percent in fiscal year 2010 and employment is not expected to grow at all in fiscal year 2011, personal income is expected to grow in fiscal years 2011 and 2012, averaging between two and three percent. Nonagricultural employment in fiscal year 2010 fell 3.3 percent. Inflation is expected to remain below two percent in fiscal years 2011 and 2012.

General fund revenue estimates have not changed substantially from the July 2010 estimate. The estimate for fiscal year 2011 totals $5.11 billion, which is three percent less than fiscal year 2010. Recurring revenues to the fund are projected to grow by six percent from fiscal year 2010 levels; however, federal stimulus funding from fiscal year 2010 is no longer available for the current fiscal year. Total revenues to the general fund in fiscal year 2012 are expected to be $5.36 billion, a five percent increase from the current fiscal year. Annual growth to general fund revenues are expected to be at four percent during fiscal years 2013 through 2015.

Mr. Clifford then presented the LFC's analysis of the revenue estimate. The key points of the analysis include:

- Fiscal year 2010 revenue was $172 million less than appropriations.

- Fiscal year 2011 revenue, after authorized reserve transfers and allotment reductions of $151 million, is $17 million less than appropriations.

• Fiscal year 2012 revenues are predicted to be $258 million below the cost of current services. Those revenues include the replacement of $350 million in federal Medicaid and public school funds.

• While general fund recurring revenue fell by more than 20 percent from fiscal years 2008 to 2010, total spending, including federal temporary funding, actually increased during those years.

• Gross receipts tax (GRT) revenue declined by more than 10 percent in fiscal year 2010. GRT revenue is expected to increase by three percent in fiscal year 2011 and by four percent in fiscal year 2012.

Questions and comments from committee members included the following:

• The projection of personal income tax (PIT) growth over the next few fiscal years seems overly optimistic. Sam Flame, chief economist, DFA, said that the indicators predict that New Mexico should be seeing increases in employment, which correspond to PIT levels.

• New Mexico tends to enter and exit from recessions later than the rest of the nation. Mr. Clifford agreed, and he said that he prefers to use employment trends in addition to GDP levels. He said that increases in oil and gas production do not necessarily mean that more jobs are created. New Mexico has not yet reached positive growth in employment, but the rest of the country did so several months ago.

• Many of the cuts to public education in the past two years have been more than offset by federal Title 1 and stimulus funding, which is distributed directly to school districts. Some districts have realized unprecedented levels of funding. DFA and LFC staff were asked to provide a listing of total funding for public schools, not just general fund appropriations.

• Did the consensus revenue economists assume zero percent economic growth in the next fiscal year? Mr. Clifford said that the fiscal year 2012 scenario is essentially a no-growth estimate.

• Why did the corporate income tax (CIT) revenues show such a strong growth? Mr. Clifford likened the CIT growth, from almost nothing to a small amount, to the observation that "even a dead cat will bounce".

• If the legislature replaces temporary federal funding, that will make the services provided permanent.

Laboratory Partnership with Small Business Tax Credit — Annual Report

Genaro Montoya, program leader, New Mexico Small Business Advocates (NMSBA), Sandia National Laboratories, and Mariann Johnston, Los Alamos National Laboratory (LANL), presented the annual report of the laboratory partnership with small business tax credit program to the committee. Mr. Montoya stated that the NMSBA is a catalyst for the transfer of cutting-edge technology from the state's national laboratories to a wide range of small businesses across the state. The tax credit allows each national laboratory to claim up to $2.4 million per year in expenses for assisting small businesses. Rural businesses are allowed up to $20,000 per year in assistance, and small businesses in urban counties can receive $10,000 in assistance.

Between 2000 and 2009, $20.6 million in assistance was provided to 1,597 small businesses in 32 of the state's 33 counties. So far in 2010, $4.2 million in assistance has been provided to 301 small businesses. The NMSBA studies the economic impact of the tax credit. It estimates that 1,549 jobs in 2010 were created or retained as a result of the business assistance. The return on investment realized by the state from the credit is estimated to be $1.24 for every dollar of credit.

Ms. Johnston described different industries that are benefiting from the assistance provided by the laboratories. The NMSBA is helping companies develop technologies to treat and reuse produced water from oil and gas operations. Businesses in the Roswell area are also getting help in developing technology to more precisely locate bypassed petroleum deposits in the Permian Basin. The NMSBA is helping the renewable energy industry by assisting with biofuel production, solar thermal and wind turbine design improvements and evaluation of landowner potential for wind and solar energy generation, production and distribution. The NMSBA is also helping the agricultural industry: providing assistance on projects to manage surface water quality, reservoir storage and water delivery schedules; developing a new bovine tuberculosis test; treating ground water for high sulfates to protect cattle health and reproduction; and developing tools to differentiate between dairy and nondairy contributions to nitrate contamination in ground water.

Ms. Johnston introduced Jay Lazarus, owner of Glorieta Geoscience, a ground water consulting company. The company has received technical assistance from LANL to perform forensic research on dairy isotopes to specifically identify nitrate contamination sources. Many feedlot dairies are under ground water contamination abatement orders by the Department of Environment (NMED), and if the nitrate contamination from previous chemical fertilizer use can be differentiated from the current nitrate contamination from the dairies, the industry could get relief from the strict requirements. LANL is helping Glorieta Geoscience develop its technical capabilities to identify those nitrates, he said.

Committee members lauded the laboratories for their exemplary work in assisting small businesses in New Mexico.

Business Incentives Most Commonly Used for Economic Development

The committee heard from a panel of business owners and leaders about important business incentives. Larry Horan, lobbyist, Eastern New Mexico Economic Development Association, introduced the members of the panel and said that the panel's intention was to educate the committee about the most important statutory business incentives and how they are being used.

Pat Vanderpool of Tucumcari Economic Development said that the goal of economic development organizations is to increase employment and income in communities through business recruitment and retention efforts. The most important business incentive is the job training incentive program (JTIP), which provides training funds for new employees. Other important incentives include the high-wage jobs tax credit and the investment credit. The economic development community needs to use every tool available to attract and retain businesses, he said.

Debra Inman of Albuquerque Economic Development discussed three potential business relocations that Albuquerque recently lost. Soladyne Capital, an insulated-glass manufacturer, recently decided to locate a facility in Mississippi instead of New Mexico, partially because better incentives were offered by that state. The state also lost an opportunity to Michigan when Suniva, a photovoltaic manufacturing company, decided to locate there. A third company, whose name has not yet been disclosed, recently decided not to locate in New Mexico, costing the state 500 jobs.

Doug Penner of Altela, a company specializing in water desalinization and produced water purification, discussed the incentives of which his company has taken advantage. Altela started operations in 2005 and has 25 employees. Prior to the recent economic downturn, the company had 50 employees. Currently, the company is in a gradual hiring phase. Altela uses JTIP funding, the high-wage jobs tax credit, the investment credit and the technology jobs tax credit.

Brenda Miller, director of human resources, Southwest Cheese, told the committee that her company located in New Mexico instead of Texas because of the incentives New Mexico provided as well as the long-term advantages the state offered. Southwest Cheese has 324 employees and processes 11 million pounds of milk per day. New Mexico now ranks seventh in the nation in milk production, and the state has surpassed Wisconsin in cheese production. The company uses JTIP funding, the high-wage jobs tax credit and industrial revenue bonds.

Brandon Honea of the global tax, audit and advisory firm KPMG said that he performs site selection services for clients seeking to locate their businesses. The firm performs comparative analyses and modeling of the business climate in different states, including the level of tax incentives available. KPMG was responsible for bringing the Hewlett-Packard call center to New Mexico, creating 1,800 jobs. He said that tax credits make a good site better, but they do not make a poor site into a good one. Nationally, two kinds of incentives work well in attracting businesses: cash grants and payroll tax credits. New Mexico has a very competitive set of incentives, and he recommended that those incentives be continued.

A committee member commented that the legislature does not appreciate it when companies come to New Mexico for a few years and then leave for better pastures in other states. Call centers have earned a poor reputation in rural areas. The committee member also said that industrial revenue bonds have the effect of raising property taxes on everybody else.

Property Tax Legislation — Fiscal Impact Report Review

Mr. Clifford and Julie Anna Golebiewski, senior economist, LFC, presented to the committee a review of property tax "lightning" legislation introduced in the last regular session of the legislature. Property tax lightning refers to large differences in the property tax valuation of two otherwise similar properties. Section 7-36-21.2 NMSA 1978 limits the annual growth in valuation of certain properties to three percent per year. Other properties, especially properties that change owners, are assessed at the full market value. If the market value of properties grows more than an average of three percent, the disparity between valuations grows over time. Ms. Golebiewski began with an overview of the legislation. Both retroactive and prospective remedies were proposed, with a wide variety of fiscal impacts. With all of the legislation, some taxpayers would see tax increases and some would see decreases. The constitutional status of the current law, as well as the new proposals, remains uncertain.

A survey of other states' laws regarding property tax lightning showed that 20 states have some kind of valuation limitations. Most of those states restrict the annual growth rate to between two percent and 15 percent. Some states do not require the correct valuation of properties upon sale.

Mr. Clifford discussed some of the issues addressed by the seven property tax lightning bills in the previous legislative session. All of the bills proposed equal treatment of property valuations prospectively, at least for existing properties. Prospective remedies do not address the existing gap from differential valuations from 2004 to the present.

Two bills proposed retroactive remedies by bringing all assessed values to today's market values, then applying growth limits in the future. The LFC estimated that this would cause a 14 percent increase in statewide residential taxable value in the first year. Properties that currently enjoy limitations in valuations would see a five to 10 percent increase in tax payments, while those properties currently valued at market values would see a 10 to 15 percent decrease in property tax payments. In addition, the statewide general obligation bond capacity would increase by approximately $40 million.

Two bills proposed retroactive remedies by lowering the assessed values of properties sold after 2004 to a rate not exceeding three percent per year. The LFC estimated that this method would result in an average six percent increase for currently limited property owners.

Another bill proposed limiting valuations only to the constitutionally mandated categories of age, income and owner occupancy, rather than having statutory limitations that provide no distinction between owner-occupied and rental properties. In order to implement this provision, county assessors would need to obtain accurate data on the residency status of properties.

One bill attempted to address valuation disparities that happen between new construction and existing properties by adjusting new construction assessments toward existing properties' assessed valuations. The problem with this approach is determining how to find comparable properties for valuation purposes.

Overall, the fiscal impact of most of the bills would be that the current beneficiaries of valuation limitation would see increases in their property taxes, but government revenue would be generally the same. However, some governmental entities that are currently at their maximum rate level could see revenue decreases, but those impacts would be small. All bills would reverse the inequity that exists in current law.

Questions and comments from committee members included the following:

• How do New Mexico's property taxes rank in comparison to other states? Mr. Clifford said that the state ranks pretty low nationally, but Bernalillo County property taxes are about twice that of the rest of the state.

• There is a policy disagreement about whether new construction should be valued at its market value when it enters the tax rolls, or whether comparable values should be used.

• How will the new real estate transaction fees for Medicare, recently enacted by Congress, affect homeowners in New Mexico? Mary Martineck of the New Mexico Realtors Association said that she would provide the committee with information on that new tax. She said that most real estate transactions would not be covered by the new law. (The following day, she presented a fact sheet that stated that real estate sales that result in a net capital gain above $250,000 for individuals who have an adjusted gross income above $200,000 would be subject to a 3.8 percent tax on those capital gains above $250,000, beginning in 2013.)

Property Tax — Issues and Proposals

The committee heard a presentation and discussion of solutions to the property tax lightning problem. James P. O'Neill, consultant, began the presentation by reminding the committee that Article 8, Section 1 of the Constitution of New Mexico requires the legislature to enact property tax valuation control. Any solution enacted to fix the current problem with Section 7-36-21.2 NMSA 1978, portions of which were determined by two district judges to be unconstitutional, will necessarily make a portion of residential homeowners pay higher property taxes. He cautioned against a solution that would reduce or hold harmless property taxes for all residential properties because county governments rely almost completely on property tax revenues for their budgets.

Gary Perez, Dona Ana County assessor, discussed two legislative solutions developed by the New Mexico Association of Counties (NMAC) President's Property Tax Committee. He said that the goal of assessing similar properties similarly directly conflicts with the goal of insulating long-term homeowners from the tax effects of market increases. There are several sections of law that need to be considered in order to understand the situation. Section 7-36-16 NMSA 1978 requires county assessors to maintain current and correct valuations of property. However, Section 7-36-21.2 NMSA 1978 limits to no more than three percent the annual valuation increases of certain classes of residential property. Section 7-36-21.3 NMSA 1978 provides for no property valuation increases for low-income elderly or disabled homeowners. Section 7-37-7.1 NMSA 1978 limits the increase of property tax revenue to no more than the percentage increase from new construction plus inflation. This provision is commonly referred to as "yield control".

The first option, which is the most favored choice of county assessors, would be to amend Article 8, Section 1 of the Constitution of New Mexico to eliminate the mandatory limits on valuation. If the amendment is adopted by the voters in 2012, then the legislature would eliminate or increase the annual valuation cap; require county assessors to bring all property valuations to their market value; and set the yield control inflation factor to zero for the first year, which would have the effect of maximizing the rate-reduction effect. This method would establish a permanent process for equalizing valuations and would not discriminate against new construction. However, property taxes would rise significantly for those properties that are undervalued.

The second option would consist of statutory changes only and is the choice of the NMAC committee. County assessors would bring all property valuations to current and correct levels; the yield control inflation factor would be set to zero; and the valuation cap would be converted from a full value cap to a taxable value cap, perhaps set at a different percentage increase level. The last provision would allow the full valuation of properties to be displayed, along with the taxable value of those properties, and would allow county assessors to maximize the use of computer-aided mass appraisal (CAMA) systems. This solution has the same drawback as the first solution: long-term residential homeowners would see significant increases in valuation and tax assessments.

Questions and comments from committee members included the following:

- Committee members expressed their desire to meet with the key stakeholders in this issue.

- Some counties do not have CAMA systems. Would this become a barrier to the implementation of either solution? Mr. Perez said that either option can occur with current technology. He said that the NMAC committee is looking for direction from the RSTP about which option to pursue in the upcoming legislative session.

- When the current three percent valuation limitation was enacted, county assessors were supposed to bring all property valuations to current and correct levels before imposing the limitation, but that did not happen. What assurances are there that they would bring properties to the correct level if new statutory changes are made? Mr. O'Neill said that the requirements of valuations would need to be specified in the legislation.

- Glenn Walters, county commissioner, Sandoval County, said that fixing the property tax lightning issue is the top legislative priority of the NMAC. He acknowledged that adopting a constitutional amendment would be difficult.

- Any solution to the property tax lightning problem needs to address the decade-long overpayment of property taxes by some homeowners.

- Both options would need a phase-in period to make them palatable to homeowners.

- Any solution to the property tax lightning problem needs to ensure that there will be no net increase in tax revenue to local governments during the transition period.

- Staff was directed to ask for an attorney general's opinion on whether the legislature can roll back property tax valuations to previous levels. Mr. Perez said that there is also a language disparity between the constitution and statutes between "owner-occupied" and "residential" that should be remedied.

Mr. O'Neill then presented a proposal to clarify the calculation of mill rates pursuant to the yield control law (Section 7-37-7.1 NMSA 1978). The primary change in the law would be to differentiate the calculation of "net new value" and "valuation maintenance". This change would allow counties to set mill rates much easier than with the current system.

Al Maury, senior policy analyst, TRD, briefly presented an update to the committee of recent property tax data. Net taxable value of all property in New Mexico's tax system in 2010 is approximately $50.5 billion. This value is 7.2 percent less than the total taxable value in 2009. The drop in values is almost entirely due to the large decline in oil and gas production, which determines the amount of ad valorem and equipment property tax paid. Residential and commercial valuations increased an average 1.3 percent from 2009. In 2010, tax obligations are estimated to be $1.5 billion, which is four percent less than in 2009. The average mill rate for all properties in 2010 is 28.8 mills, which is three percent higher than in 2009.

Counties received 51 percent of their total revenues in 2009 from property taxes, compared to 24 percent from GRT revenue. In contrast, municipalities received 70 percent of their revenue from GRT distributions and only nine percent from property taxes. Statewide, growth diminished over the last three years in almost all of the state's major revenue sources, except property taxes.

Mr. Maury discussed the lack of useful data available for state agencies to evaluate property tax issues. Certain data are provided to the TRD by each county assessor, but what is provided is usually insufficient. The TRD needs accurate individual data from each county, including assessed values, number of years of current ownership, when the properties sold, etc.

The committee recessed at 5:00 p.m.

<u>Tuesday, October 26</u>

The committee reconvened at 9:18 a.m. on Tuesday, October 26, 2010. The minutes from the August and September meetings of the committee were adopted without changes.

Manufacturing, Distribution and Logistics on the Border — PIT Credit

Juan Massey, director, regulatory affairs, Verde Realty, and Jerry Pacheco, vice president, Border Industrial Association, presented proposed changes in the law to expand PIT credits for residents of Texas who commute to New Mexico in the international border region. Currently, workers who work within 20 miles of the border with Mexico and are employed by certain manufacturing industries are allowed to be taxed at the rate that Texas imposes, which is currently zero. The new legislation proposes to expand eligible industries to include distribution and logistics businesses, and it changes the incentive into a PIT credit of up to $1,000 annually.

Mr. Pacheco said that this legislation is necessary because it is very difficult to get companies to relocate to the Santa Teresa area, from just across the Texas border, because of the PIT in New Mexico. Employees would prefer to stay in El Paso and not pay income taxes. In 2001, the legislature essentially exempted from the PIT workers commuting from Texas who work in the manufacturing industry. By expanding the exemption (now a credit) to the distribution and logistics industry, the Santa Teresa area stands to see a major surge in economic development.

Mr. Massey said that the new law would provide the PIT credit for 10 years; the maximum credit is $1,000, rather than unlimited; and companies using the credit would be required to increase their New Mexico employee payroll by 10 percent each year. He said that employee recruitment of New Mexico residents in the area has been challenging due to the high poverty rate, the lack of education of many residents and the lack of public transportation. He said that many distribution companies currently cross the international border at Santa Teresa and then drive into Texas to unload their product. The proposed legislation would attract large distribution companies to relocate to New Mexico.

Questions and comments from committee members included the following:

• Why bring in several hundred Texans to work in New Mexico businesses rather than provide education to the New Mexico work force? Mr. Pacheco said that training programs exist in the area, but there is a serious lack of qualified workers from New Mexico. He cited statistics that show that 37 percent of the potential workers in the area do not have a high school diploma.

• How will the credit help unemployed New Mexicans? Mr. Pacheco said that more time is needed to provide education and training to the local population. Companies using the credit would be required to increase their New Mexico work force by 10 percent each year.

• Instead of spending $1,000 per worker from Texas, why does the state not spend that money to provide better education to the New Mexico work force? Mr. Pacheco said that the PIT is the biggest obstacle in attracting Texas businesses to the Santa Teresa area.

• The legislature recently enacted a tax credit for train fuel, which benefited Verde Realty tremendously.

• The state needs tax policies that attract manufacturing businesses for the long term. Texas, facing a huge budget shortfall, will probably raise taxes, which will make New Mexico a more attractive business climate.

Use of Alternative Energy Tax Credits

Annie Carmichael, lobbyist, Sun Edison, reviewed the key tax policies in New Mexico that support solar energy development. Sun Edison is a global solar energy production and development company, with more than 380 plants in operation. The company focuses on retail and wholesale distributed generation, from roof-top generation facilities to large facilities producing many megawatts (MW).

A long-term, pro-solar-energy state policy is key to attracting companies like Sun Edison, said Ms. Carmichael. Property tax reductions, sales tax abatement and PIT and CIT solar production tax credits are the most common tax incentives that states provide to attract companies. New Mexico ranks very high among other states in solar energy incentives, and she encouraged the committee to keep those incentives intact.

Questions and comments from committee members included the following:

• What is the total dollar impact to the state of the new 50 MW facilities in southeastern New Mexico? Ms. Carmichael said that she will report that information to the committee. She estimated that 20 long-term jobs will be created once the construction phase is complete.

• What factors are limiting solar energy development in the state? Ms. Carmichael said that now that third-party financing is allowed for solar energy facilities, there really are no more obstacles.

• Sun Edison should obtain photovoltaic panels from New Mexico for its New Mexico projects.

Jet Fuel GRT Credit Sunset

Ed Mahr, lobbyist, Southwest Airlines, presented to the committee legislation to extend the current deductions from gross receipts and from compensating tax due for the sale of jet fuel in the state. Fifty-five percent of the value of the jet fuel is allowed to be deducted, and after July 1, 2012, the deduction amount is scheduled to be reduced to 40 percent. The proposed bill extends the 55 percent deduction level until 2017.

Southwest Airlines purchases jet fuel from three main sources, 40 percent of which is produced in New Mexico. The fuel is trucked and pumped through pipelines to Albuquerque from different locations. Mr. Mahr said that jet fuel is the second-highest expense of the airline, after personnel. Keeping the deduction at the 55 percent level will keep New Mexico somewhat competitive with other states. The airline industry is critical to the state's economy, he said.

Other options in addition to extending the sunset date for the jet fuel deduction would be to make the deduction 100 percent or to have no sunset of the deduction. The best option, however, would be to convert the GRT on jet fuel into a unit tax, based on volume rather than price. A unit tax would be much less volatile than the current GRT on the price of jet fuel.

Federal Low-Income Housing Credit Use in Valuation of Property

Steve Natelson, attorney, and Representative Gonzales presented legislation for the committee's consideration that would ensure that the value of federal affordable housing tax credits does not get calculated in the valuation of properties for property tax purposes. The New Mexico Mortgage Finance Authority (MFA) administers the federal tax credits, which are issued to property developers on a competitive basis. The purpose of the credits is to make the construction of low-income housing affordable; without the credits, it is not cost-effective to build most low-income housing.

Mr. Natelson represents the owner of an affordable housing project in Taos County who protested the valuation of the property by the county assessor. The county assessor attempted to value the property using the tax credit as a basis for valuation of the property. The TRD has never issued any regulatory guidance on this issue, and Taos County is the only county in the state to use such a valuation method. In addition, Section 7-36-15 NMSA 1978 requires the assessor to take into consideration the decrease in market value of an affordable housing property if it were to sell. This requirement, in essence, requires the assessor to factor in the rents charged to residents because federal law restricts the future use of those properties to affordable housing clients. The Taos County Valuation Protests Board ruled against the property owner, and the decision has been appealed to the district court. If the decision of the board stands and the new method of valuing affordable housing property spreads to other counties, there will be a chilling effect on affordable housing projects.

Questions and comments from committee members included the following:

• The committee should send a letter to the Property Tax Division of the TRD requesting that the division adopt a rule providing guidance to county assessors on this issue.

• Did the county assessor use rents in valuing the property? Steve Croiser, the developer of the property, said that the assessor used market-based rents, rather than the federally required contract rents, to determine the value of the property.

• Did Taos County provide land for the project, and how close was the MFA application estimate to the actual costs? Mr. Croiser said that the land was purchased at market value. In affordable housing projects, the return to the investor is generated by the federal tax credits. Valuing the property based on its replacement cost or potential sale cost does not work.

• What was the developer's original appraisal for the property? Mr. Croiser said he did not remember; he will provide that information to the committee. He said the total cost for the project was approximately $7 million. The annual income from the development is about $240,000. There are 56 units, and the average rent is $400 per month. Each year, the MFA develops an allocation plan, which determines project needs in each geographic area of the state. Developers then submit applications to the MFA for projects.

• Developers of low-income projects should not receive any special property tax treatment.

• How much do residents pay in rent? Representative Gonzales said that rents are determined based on family incomes. About 25 percent of the units at the development in Taos have rents provided by the federal government. Rents are typically $400 to $600 per month lower than full-market rent levels.

• County assessors in the audience were asked to comment on the correct method of valuation to use in affordable housing projects. Clyde Ward, county assessor, San Juan County, said that the three valuation approaches, sales of comparable properties, income and cost, are used. The cost approach and the income approach do not match up in this case, he said. Joaquin Valdez, county assessor, Los Alamos County, said that he uses all three methods of valuation and chooses the method that best suits a particular property. He said that Los Alamos County treats subsidized housing the same as regular housing properties.

• Why do county assessors have so much latitude in valuing properties? Mr. Natelson said that statute already requires county assessors to take into account the decrease in value of affordable housing projects. The Taos County assessor decided to use a brand new methodology to value those properties, without any statutory or regulatory authority.

Above-Ground Storage Tanks

Senator Sapien, Cyndee Biggers, petroleum distribution manager, Bowlin Travel Centers, and Scott Scanland, lobbyist, Bowlin Travel Centers, presented a bill to the committee that would provide CIT and PIT credits for 50 percent of the cost of complying with NMED requirements for upgrading above-ground fuel storage tanks. Senator Sapien said that he introduced Senate Bill 253 in the last regular legislative session to provide a similar credit for compliance.

Ms. Biggers said that Bowlin Travel Centers operates seven facilities. Two of those facilities have ceased providing gasoline to retail customers because the company determined that the cost of compliance with NMED rules is too high. The NMED has mandated that storage tanks be double-walled or that secondary collection areas be installed according to NMED specifications. The company has completed upgrading one facility, at a cost of $120,000. The department has set a July 1, 2011 deadline for facilities to comply with the rule. She asked the committee to support the legislation, which would partially offset the cost of compliance.

Ruben Baca, executive director, Independent Petroleum Marketers Association, said that complying with the new rule has been a problem for many companies. Of the 1,300 above-ground storage tanks in the state, only 300 are currently in compliance.

Mr. Scanland said that the NMED rules are a huge unfunded mandate. Many of these tanks were installed in order to comply with previous stricter rules governing underground storage tanks at significant expenses to the property or business owners. Now they are being asked to upgrade those new tanks at an additional and considerable expense. It would be easier to allow the owners to allow the new tanks to remain for their life and change to the newer provisions when replacement of the tanks becomes necessary.

Senator Sapien said that there are many small businesses that cannot afford the cost of compliance, and they will be forced out of the business of selling gasoline.

Questions and comments from committee members included the following:

• Instead of providing a tax credit, the legislature should enact a moratorium on the storage tank rule.

• What is the estimated fiscal impact on the state of the credit? Senator Sapien said that it will cost the state $6 million, which will probably be offset by the tax revenue the state will receive if these businesses continue to operate.

• New tax credits are difficult to justify in the current economic downturn. The NMED rule should be repealed instead.

• Some state agencies have overly broad statutory authority to adopt rules. Mr. Baca said that New Mexico is the only state in the nation that regulates above-ground storage tanks.

• The Government Restructuring Task Force will probably endorse a bill that gives the legislature the ability to review agency rules.

• In 1989, the legislature provided that a portion of the proceeds of the petroleum products loading fee be deposited into the Corrective Action Fund to help with the costs associated with replacing underground storage tanks. However, the legislature recently enacted a law that redirected that portion of the tax for other purposes. This distribution should be used to help with the compliance costs of the above-ground storage tank rule. Mr. Baca said that redirecting the tax would provide about $6 million annually.

• Maybe the NMED rule should be amended to require double-wall tanks on new installations only.

There being no further business, the committee adjourned at 3:22 p.m.