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

SPONSOR Nava **ORIGINAL DATE** 02/07/11 **LAST UPDATED** 03/08/11 **HB** 523/HTRCS

SHORT TITLE Locomotive Fuel Tax Gross Receipts Deduction **SB**

ANALYST Golebiewski

REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Non-Rec	Fund Affected
FY11	**FY12**	**FY13**		
		No effect until FY14	Recurring	Counties, Municipalities, and General Fund

(Parenthesis ( ) Indicate Revenue Decreases)

SOURCES OF INFORMATION
LFC Files

Responses Received From
Taxation and Revenue Department (TRD)
Economic Development Department (EDD)

SUMMARY

Synopsis of Bill

House Bill 523 would provide a deduction from the gross receipts tax (GRT) and compensating tax for locomotive fuel beginning on July 1, 2013, contingent on certification by Economic Development Department that the construction of a railroad locomotive refueling facility project in Dona Ana County has commenced by July 1, 2012.

Eligibility for the deduction would be limited to a railroad that after July 1, 2011 “made a capital investment of $100 million or more in new construction or renovations at railroad locomotive refueling facility in which the fuel [is loaded, used, or sold.]”

The bill also describes the purpose and requirements of the locomotive fuel deduction, such that the Economic Development Department (EDD) can measure the effects of the deduction. EDD is required to compile an annual report containing information on those who claim the deduction, the number of jobs created as a result of the deduction, and the amount of the tax expenditure – all information will be required to be provided by the relevant taxpayers to both TRD and EDD. This report is to be used to evaluate the effectiveness of the deduction.

FISCAL IMPLICATIONS

Estimated Revenue Impact*					R or NR**	Fund(s) Affected
FY2011	FY2012	FY2013	FY2014	FY2015		
0	0	0	($186.0)-($1,686.0)	($191.0)-($1,691.0)	R	Counties
0	0	0	($286.0)	($294.0)	R	Municipalities
0	0	0	($1,387.0)-($5,887.0)	($1,426.0)-($5,926.0)	R	General Fund
0	**0**	**0**	**($1,858.0)-($7,858.0)**	**($1,910.0)-($7,910.0)**	**R**	**Total**

** In thousands of dollars. Parentheses ( ) indicate a revenue loss. ** Recurring (R) or Non-Recurring (NR).*

TRD:

This estimate was made using information from the Surface Transportation Board including fuel use, fuel costs, and track miles operated for Class I railroads operating in New Mexico. Data from taxpayer reporting, the consensus revenue group's oil price forecast, and a freight transportation forecast from the Global Insight forecasting service were also used. <u>If a locomotive refueling facility would have located in New Mexico without the proposed deduction then the fiscal impact would be almost $6 million greater totaling approximately $7.8 million in FY 2014.</u> [It should be noted that the State Land Office has reported that Union Pacific owns the land on which it proposes to build.]

The Department cannot clearly determine if Union Pacific's Strauss/Santa Teresa Facility would go ahead in the absence of the proposed deduction. The [lower bound of the] estimated revenue impact shown in the table on page one assumes that the proposed facility would <u>not</u> be completed in absence of the new deduction. Under this scenario, the loss in revenue of this bill would only be equal to the compensating tax revenue lost from locomotive fuel used within New Mexico but bought outside of New Mexico without paying tax to another state.

If the facility would actually be completed in absence of the new deduction, the revenue impact of this bill would be significantly greater. In that scenario New Mexico would be giving up any locomotive fuel still subject to the compensating tax and also any gross receipts revenue from fuel purchased in New Mexico and loaded into locomotives in New Mexico. The estimated revenue loss under this scenario would be approximately $7.8 million in gross receipts and compensating tax in FY 2014 growing to $8.0 million in FY 2015.

In either scenario, the revenue loss is recurring each year and continues to grow along with the price of diesel and the volume of railroad freight traffic.

SIGNIFICANT ISSUES

TRD:

The proposal creates a trade-off between targeted economic development and the tax policy goals of simplicity, efficiency and equity. Eliminating GRT on fuel purchases is an important incentive for railroads to locate their refueling facilities in New Mexico.

> However, by narrowing the tax base, the proposal puts upward pressure on tax rates, increasing negative impacts of the tax system on the New Mexico economy. This proposal would increase the divide between how fuel used for truck transportation and fuel used for rail transportation is taxed in New Mexico. Currently diesel fuel used for trucking is taxed under the fuel taxes at 22.875 cents per gallon[1]; whereas, fuel used for rail transport is taxable under either the GRT or compensating tax (equivalent to roughly 10 cents per gallon in FY 2010). Not treating similar business activity the same violates the equity principal of good tax policy. This bill has a non-tax policy goal to stimulate the railroad industry in New Mexico that should be evaluated with the same framework used for spending choices such as performance budgeting criteria.

As noted by TRD in their evaluation, it is unclear whether Union Pacific would locate their facility in New Mexico in the absence of the credits. Ideally, tax incentives would be offered to entice businesses who would not otherwise locate in New Mexico to locate here. If they would locate here regardless of the credit, the amount of the credit would be an unnecessary expenditure of state funds.

As noted by the Economic Development Department (EDD), "the Union Pacific Railroad (UPRR) proposes to begin construction of a $300 - $400 million rail expansion project in 2011…[including] a mainline refueling station, train inspection area, crew change facilities, and block swap and switching yards initially employing 300 or more persons." UPRR also estimates that as many as 3,000 workers will be employed in construction of the facilities.

The feedback effects of this policy are not incorporated into the fiscal impacts shown above. These could be substantial given the size of the construction project and refueling facility, but the estimates would be highly uncertain. In addition, if the station would be located in New Mexico even in the absence of the deduction, the feedback effects of HB 523 on the state would be zero (because they would have occurred anyway).

ADMINISTRATIVE IMPLICATIONS

TRD:

> Tracking and reporting on the deduction will be complicated for the taxpayer and the Department. The bill states that the purpose of the deduction is to "encourage the construction, renovation, maintenance and operation of railroad locomotive refueling facilities and related activities in New Mexico." However, the targeted beneficiaries of the deduction are not actually the taxpayers taking the deduction because the GRT deduction is claimed by the <u>seller</u> not the buyer of the fuel, but the buyer is the target of the incentive. Assuming the seller has other taxable transactions in New Mexico, tracking this deduction will require separate reporting, which will have to be processed outside the Department's information systems. This type of manual reporting is slow and expensive, and creates added risks of creating errors and delaying distributions. Although the goal of increasing transparency of economic development incentives is a desirable one, if the Department is required to separately track all exemptions and deductions in the GRT, the current information system will be inadequate to the task, and

[1] Diesel fuel used in trucking is subject to the special fuel tax at 21 cents per gallon and the petroleum products loading fee at 1.875 cents per gallon.

the likelihood of delays and errors in revenue collection and distribution will increase significantly. This information is based on the Department's experience with the separate reporting of the food and medical GRT deductions, which created numerous problems with GRT distributions.

TECHNICAL ISSUES

TRD:

The reporting requirements that this proposal places on the Department that include disclosing taxpayer information are in direct conflict with the general confidentiality statutes under Section 7-1-8 NMSA 1978. The general confidentiality statutes carry criminal penalties including imprisonment for up to one year. Without amending the general confidentiality statutes in Section 7-1-8, it is likely that the Department will not be able to comply with the reporting requirements. For example, the likelihood is that there will be a small number of eligible taxpayers claiming the deduction. Even if the Department were to publish only the total amount of the deductions claimed, this could compromise taxpayer confidentiality. Also on page 2, line 16, "related activities" should be defined.

JAG/bym

The Legislative Finance Committee has adopted the following principles to guide responsible and effective tax policy decisions:

1. ***Adequacy:*** *revenue should be adequate to fund government services.*
2. ***Efficiency:*** *tax base should be as broad as possible to minimize rates and the structure should minimize economic distortion and avoid excessive reliance on any single tax.*
3. ***Equity****: taxes should be fairly applied across similarly situated taxpayers and across taxpayers with different income levels.*
4. ***Simplicity***: *taxes should be as simple as possible to encourage compliance and minimize administrative and audit costs.*
5. ***Accountability/Transparency:*** *Deductions, credits and exemptions should be easy to monitor and evaluate and be subject to periodic review.*

More information about the LFC tax policy principles will soon be available on the LFC website at www.nmlegis.gov/lcs/lfc