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

ORIGINAL DATE 1/24/2020
SPONSOR Small **LAST UPDATED** 2/10/2020 **HB** 50/a HFl#1

SHORT TITLE Amending the Industrial Revenue Bond Act **SB**

ANALYST Graeser

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY20	FY21	FY22	FY23	FY24		
			Probably ($0.0)		Recurring	General Fund, GRT & compensating tax
			Probably ($0.0)		Recurring	Local Governments, GRT & compensating tax
			About ($68.0)	About ($63.0)	Recurring	State GO Bond Fund
			About $24.0	About $23.0	Recurring	State GO Bond Fund 5 percent of in-lieu payments
			About ($660.0)	About ($618.0)	Recurring	Local Governments, property tax debt and operating
			About ($484.0)	About ($452.0)	Recurring	School Districts, property tax debt and operating
			About ($139.0)	About ($130.0)	Recurring	Higher Ed, Hospital, SWCD Districts, property tax debt and operating

Parenthesis ( ) indicate revenue decreases

Note: The fiscal implications of this bill are largely indeterminate. The approximate fiscal impacts are based on one $150 million transmission line completed by December 31, 2022. See Fiscal Implications for discussion. Note that there may be no GRT/comp tax impact of this proposal, at least in the short term.

Duplicates SB6

SOURCES OF INFORMATION
LFC Files
Responses Received From
Energy, Minerals and Natural Resources Department (EMNRD)
Economic Development Department (EDD)
Public Regulation Commission (PRC)

Responses Not Received From
Taxation and Revenue Department
Public Regulation Commission

SUMMARY

Synopsis of HFl#1 Amendment

The House Floor #1 amendment inserts a requirement in two places in the bill that, "… the school district[s] in which the project is located will receive the same amount, or greater, of annual in-lieu tax payments as would have been received in property taxes for the fully developed project had the project not been acquired."

Synopsis of Original Bill

House Bill 50 amends the Industrial Revenue Bond Act (§§3-32-1 et seq. NMSA 1978) and the County Industrial Revenue Bond Act, (§§4-59-1 et seq. NMSA 1978) to include electric transmission facilities as eligible projects. The bill adds a new section to each Act that requires for electric transmission line projects the state would receive 5 percent of the total amount of in-lieu tax payments to counties, municipalities and other local entities who levy taxes on the property. This also includes in-lieu tax payments to school districts and 5 percent of the value of other considerations paid by the transmission line project managers to local entities that are authorized to levy taxes on property. A copy of the agreement documenting the in lieu payments must be provided to the secretary of finance and administration with 30 days of written approval. Annual payments are to be made to DFA for deposit to the general fund no later than the end of the fiscal year as in-lieu tax payments are made to local taxing entities.

The effective date of this bill is July 1, 2020. There is no delayed repeal but LFC recommends adding one. This is an unusual tax expenditure and a delayed repeal date would give the legislature an opportunity to review the success or failure of the proposal.

FISCAL IMPLICATIONS

This bill may be counter to the LFC tax policy principle of adequacy, efficiency, and equity. Due to the increasing cost of tax expenditures, revenues may be insufficient to cover growing recurring appropriations. This particular tax expenditure affects county governments and school districts more than the state, although the abatement of compensating taxes could be significant for the general fund.

This bill creates or expands a tax expenditure with a cost that is difficult to determine but likely significant. LFC has serious concerns about the significant risk to state revenues from tax expenditures and the increase in revenue volatility from erosion of the revenue base. The committee recommends the bill adhere to the LFC tax expenditure policy principles for vetting, targeting, and reporting or be held for future consideration.

Estimating the cost of tax expenditures is difficult. For this bill, the difficulty is both in timing and magnitude. Confidentiality requirements surrounding certain taxpayer information create uncertainty, and analysts must frequently interpret third-party data sources. The statutory criteria for a tax expenditure may be ambiguous, further complicating the initial cost estimate of the expenditure's fiscal impact. Once a tax expenditure has been approved, information constraints continue to create challenges in tracking the real costs (and benefits) of tax expenditures.

IRBs are generally not financing tools, but tax abatement mechanisms. IRBs are built on a fiction that the tangible personal property involved in the IRB project is "owned" by the sponsoring government. Receipts from sales of tangible personal property to government can be deducted. In addition, there is no property tax on the real property and tangible personal property, again because the project's working assets are considered to be owned by the sponsoring government. This treatment extends for the duration of the bonds – limited in statute to 30 years.

The impact of this proposal on property tax revenues is relatively straightforward. There is at least one project in the pipeline (in permitting) that might qualify for property tax abatement for the full value of the project. However, the impact of this proposal on gross receipts or compensating tax abatement is not straightforward. Key to resolving this complexity is to understand that the gross receipts or compensating tax abatement would only occur if the provisions of 7-9-54 NMSA 1978 are strictly adhered to.

7-9-54. Deduction; gross receipts tax; governmental gross receipts tax; sales to governmental agencies.

A. Receipts from selling tangible personal property to the United States or New Mexico or a governmental unit, subdivision, agency, department or instrumentality thereof may be deducted from gross receipts or from governmental gross receipts. Unless contrary to federal law, the deduction provided by this subsection does not apply to: …

(3) receipts from selling construction material, excluding tangible personal property, whether removable or non-removable, that is or would be classified for depreciation purposes as three-year property, five-year property, seven-year property or ten-year property, including indirect costs related to the asset basis, by Section 168 of the Internal Revenue Code of 1986, as that section may be amended or renumbered;

According to advocates of this proposal regarding that portion of the proximate project that is currently seeking permits would be considered tangible personal property for the purposes of 7-9-54 NMSA 1978 and what portion would be considered construction material and construction-related services is that electric transmission projects would be considered 15-year MACRS property and would not qualify as tangible personal property. In 2012, the venerable construction materials GRT deduction at 7-9-52 was amended to allow a parallel deduction pursuant to this section for construction-related services. These include services such as architecture, mechanical engineering, surveying, landscape design and similar services. Thus, we can possibly narrow the 7-9-54 NMSA 1978 deduction a bit further in deciding whether a particular project is wholly construction or partly construction and partly "indirect costs related to the asset basis." LFC staff are unable to proceed from this point except to convey the impression that the expansion of the IRB statute sought in this bill will probably not result in any general fund or local government gross receipts tax or compensating tax impacts.

For the purpose of estimating an approximate property tax impact, LFC staff assume one large project would qualify within the FY21 through FY24 period. Projects that must solicit both location approval and a certificate of necessity and convenience (CNC) from PRC are not eligible for IRB treatment. In addition, there will be very few projects that have the resources to pursue this tax abatement strategy.

Rather than analyze an actual project, as was done in an earlier version of this bill analysis, LFC staff analyzed a hypothetical project to indicate an order of magnitude of the impacts of this proposal.

Data from industry sources indicate that a 345 KV above-ground transmission line costs about $1

million per mile, including design, permitting, construction materials and construction labor. This would all be considered 15-year MACRS property. Since the project is not owned by a regulated utility, it probably would not be covered by the central assessment authority of 7-36-2 NMSA 1978. However, the special assessment method of 7-36-29 NMSA 1978 would provide instructions for the specific methods to be used. For the purpose of the illustration we assume that either all of the county assessors use the same method of valuation or that TRD's central assessment bureau would take over the assessment task. Subsequent information from TRD's Property Tax Division indicate that assessors can ask for PTD to take responsibility for valuations that place an unreasonable burden on their resources or training. In this case, PTD would probably proactively inform the county assessors of the PTD's willingness to conduct the initial (and perhaps annual) assessments pursuant to the rules embedded in 7-36-29 NMSA 1978.

The hypothetical project is shown in the box to the right. It is assumed that the construction phase Gross Receipts and Compensating Tax Act taxes will have been paid. The following shows the property tax impacts in terms of revenue foregone by the exhibit project. In many cases, the sponsoring government entity (in this case, we assume five counties) will require an annual payment in lieu of taxes of some or all of the foregone property tax for school districts and, possibly, hospital, institutions of higher education, SWCD districts, etc. In this exhibit, the assumption is that the operator would pay 100 percent of the school district and special district impact as in-lieu of property taxes. The state, pursuant to provisions of the act, would receive 5 percent of these in lieu payments. This roughly equals the 1.36 state GO Bond rate divided by about an average of 25 mills for the total rate (exclusive of any debt or operating rate for municipalities). The following illustration assumes that the $150 million initial value would be depreciated using a 15-year life, straight-line depreciation and a 20 percent salvage value.

HYPOTHETICAL PROJECT
Project scope: Transmission Line: 150 miles, 345 kV
Capacity: 1,000 MW, enough to power 590,000 homes
Investment: RETA and a private developer would co-develop the $150 million project. The project would require PRC siting approval, but would be regulated by FERC as a wholesale provider in interstate commerce.
Approximate Cost: $150 million
Financial Benefit: $28 million property taxes to NM counties over first 30 years
Anticipated Operational Date: End of 2023
https://nmreta.com/transmission-lines/#impact

For Illustration, property tax revenue foregone	Property Tax Rate	Portion of Project	Annual Revenue Foregone	20-year sum	30-year sum	Net Present Value - 4%
State GO bond	1.36	100.0%	$68,000	$625,600	$761,600	$565,540
County Debt & operating						
Bernalillo County	12.223	5.7%	$34,923	$321,290	$391,136	$290,445
Santa Fe County	13.974	3.6%	$24,954	$229,573	$279,480	$207,533
Socorro County	13.385	44.3%	$296,382	$2,726,716	$3,319,480	$2,464,941
Torrance County	13.385	35.7%	$239,018	$2,198,964	$2,677,000	$1,987,855
Valencia County	12.55	10.7%	$67,232	$618,536	$753,000	$559,154
School District Debt, Operating & Special						
APS (Bern Co)	11.328	5.7%	$32,366	$297,765	$362,496	$269,178
Moriarty School District (Santa Fe Co)	10.688	3.6%	$19,086	$175,589	$213,760	$158,731
Socorro School District (Socorro Co)	10.166	44.3%	$225,104	$2,070,959	$2,521,168	$1,872,139
Estancia School District (Torrance Co)	8.125	8.9%	$36,272	$333,705	$406,250	$301,668
Moriarty School District (Torrance Co)	10.688	8.9%	$47,714	$438,971	$534,400	$396,829
Mountainair School District (Torrance Co)	6.622	8.9%	$29,563	$271,975	$331,100	$245,864
Encino School District (Torrance Co)	6.795	8.9%	$30,335	$279,080	$339,750	$252,288
Los Lunas School District (Valencia Co)	13.63	5.4%	$36,509	$335,882	$408,900	$303,636
Belen School District (Valencia Co)	10.121	5.4%	$27,110	$249,410	$303,630	$225,466
Other beneficiaries						
Hospital 1: UNM Hospital (Bern Co)	6.400	5.7%	$18,286	$168,229	$204,800	$152,078
Central NM Comm Col (Bern Co)	3.000	5.7%	$8,571	$78,857	$96,000	$71,287
Cent NM CC Debt Serv (Bern Co)	1.000	5.7%	$2,857	$26,286	$32,000	$23,762
Socorro General Hospital (Socorro Co)	4.250	44.3%	$94,107	$865,786	$1,054,000	$782,667

UNM Valencia Branch (1)	2.000	10.7%	$10,714	$98,571	$120,000	$89,108
UNM Valencia Bldg Debt Levy (2)	0.850	10.7%	$4,554	$41,893	$51,000	$37,871
Assume 5% of 100% of school district in-lieu payments to State GO Bond fund			$24,203			

The 5 percent of in-lieu property tax payments to school district to the state GO bond fund would be approximately $24,783 initially and would decline to $4,800 annually after the 15-year life.

SIGNIFICANT ISSUES

It should be noted that when a county or municipality approves an industrial revenue bond project, there are a number of tax consequences. In fact, for most projects in the state's history, the tax consequences are the principal reason a company negotiates this treatment. The IRB treatment is usually not a financing mechanism, since the bonds are amortized with payments from the commercial enterprise that has received the IRB approval.

Specifically, once the IRB treatment has been approved and construction begun, the construction is fully taxable, but the project is considered to be owned by the sponsoring government. Any equipment installed in the project is then considered tangible personal project and subject to the GRT deduction of 7-9-54 NMSA 1978. Since the real property and equipment is considered owned by the sponsoring government, the property tax exception of 7-36-3 NMSA 1978 applies. Industrial Revenue Bonds may be executed for up to 30 years.

This bill narrows the property tax base and may narrow the gross receipts tax (GRT) base. Many of the efforts over the last few years to reform New Mexico's taxes focused on broadening the GRT base and lowering the rates. Narrowing the GRT base leads to continually rising GRT rates, increasing volatility in the state's largest general fund revenue source. Higher rates compound tax pyramiding issues and force consumers and businesses to pay higher taxes on all other purchases without an exemption, deduction, or credit.

Previously, the Industrial Revenue Bond Acts provided that electric generation facilities were eligible for industrial revenue bonds. This bill expands the eligibility to also include electric transmission facilities. Neither the generation or transmission facility can be one where approvals are necessary pursuant to the Public Utility Act. This generally means that multi-state transmission lines which are regulated by FERC would be eligible to solicit IRB approvals from the various counties along the transmission line route.

HB50 creates a new concept of sharing a small portion of any in-lieu tax payments with the state. This only applies to electric transmission projects.

A perhaps partial list of currently announced electric transmission projects, with at least a portion of the line in New Mexico follows:

1. Lucky Corridor Transmission Line (Mora Line; 180 MW; 115 kV, 110 miles all in NM), (Lucky Corridor; 850MW; 345 kV; 62 miles all in NM). Real ½ million/mi (still in planning)
2. SunZia Transmission Line (500 KV; 520 miles – 315 miles in NM; 1,500 MW; $100M invested over 11 years (in permitting)
3. Southline (Hunt Power has obtained approval from PRC to move forward; uncertain current status).
4. Tuco-Yoakum-Hobbs line (345 kV; 168 miles, 63 miles in NM; $242 million; in-service in mid-2020. (The New Mexico portion has been granted a certificate of necessity and

convenience, so is not relevant to this discussion,)

5. High Lonesome Mesa (115 KV, 100 MW capacity; $50 million; 2010) RETA finish
6. Western Spirit[1] (345 KV; 1,000 MW; 140 miles; $150 million) real
7. Eddy County to Kiowa (345 KV; 34 miles in NM; $65 million) (PRC regulated, not relevant to this discussion).

Federal Regulation (FERC)

- ☐ Federal Power Act
- ☐ Wholesale sales of electricity for resale in interstate commerce
- ☐ Transmission of electricity in interstate commerce
- ☐ (Very) Limited "backstop" transmission siting authority
  See 16 U.S.C. § 824p
- ☐ Siting/Permitting of hydro plants
  Otherwise, no generation planning or siting control
- ☐ Reliability of bulk power system

State Regulation (PUCs)

- ☐ State Public Utility Acts or similar
  See, *e.g.*, VA. CODE ANN. §§ 56-235 *et seq.* and 56-576 *et seq.* (Electric Utility Regulation Act)
- ☐ Retail sales to end users
- ☐ Low-voltage distribution lines
- ☐ Siting of power plants and transmission lines
  See, e.g., MD. CODE ANN. PUB. UTIL. COS. § 7-207 (transmission and gen.)
- ☐ Resource planning; *i.e.* the generation types (coal, natural gas, renewable) used by a utility to serve customers

One of the most significant restrictions of this bill is that the transmission facility that requires both location approval and a certificate of convenience and necessity granted by the Public Regulation Commission (PRC) are not eligible for IRB treatment. The box above indicates what projects are regulated by the Federal Energy Regulatory Commission (FERC) and which are regulated by the PRC. The most important function assigned to FERC is wholesale sales of electricity for resale in interstate commerce.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

Duplicate of SB6.

OTHER SUBSTANTIVE ISSUES

Approval of Industrial Revenue projects by a county or municipal government, has fiscal consequences for the state as well as the sponsoring governments and property tax beneficiaries such as school districts, hospital districts, higher education facilities and SWCD projects. The state does not have the power to consent to the IRB treatment. School districts can negotiate all of portion of their property tax revenue foregone and request in-lieu of tax payments. The HFL amendment insures that this in-lieu payment is equal to, or greater, than it would have been absent the IRB approval. The 5 percent provision in this bill is an innovative means of

addressing this state GO bond revenue loss. However, in general, the larger state revenue loss is the loss of gross receipts and compensating tax revenue for the sale of tangible personal property to a government entity. Pursuant to the provisions of HB-6 last year, local governments will receive the local option rate for compensating tax, effective July 1, 2021. This new provision may alter the willingness of local governments to approve projects forgiving the compensating tax, and may be more aggressive in requiring in-lieu payments to the sponsoring government as well as school and special districts.

New Mexico lacks sufficient electrical transmission lines, which provides challenges to becoming a renewable energy state. IRB treatment for transmission lines could induce more renewable projects in the state. However, renewable energy produces significantly less tax revenue than fossil fuels, which poses challenges for the state in making this transition. Allowing IRB treatment for transmission lines removes a potential option for taxing renewable energy activity.

Does the bill meet the Legislative Finance Committee tax policy principles?

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

Does the bill meet the Legislative Finance Committee tax expenditure policy principles?

1. **Vetted**: The proposed new or expanded tax expenditure was vetted through interim legislative committees, such as LFC and the Revenue Stabilization and Tax Policy Committee, to review fiscal, legal, and general policy parameters.
2. **Targeted**: The tax expenditure has a clearly stated purpose, long-term goals, and measurable annual targets designed to mark progress toward the goals.
3. **Transparent**: The tax expenditure requires at least annual reporting by the recipients, the Taxation and Revenue Department, and other relevant agencies.
4. **Accountable**: The required reporting allows for analysis by members of the public to determine progress toward annual targets and determination of effectiveness and efficiency. The tax expenditure is set to expire unless legislative action is taken to review the tax expenditure and extend the expiration date.
5. **Effective**: The tax expenditure fulfills the stated purpose. If the tax expenditure is designed to alter behavior – for example, economic development incentives intended to increase economic growth – there are indicators the recipients would not have performed the desired actions "but for" the existence of the tax expenditure.
6. **Efficient:** The tax expenditure is the most cost-effective way to achieve the desired results.

LFC Tax Expenditure Policy Principle	**Met?**	**Comments**
Vetted	?	
Targeted		
Clearly stated purpose	×	No purpose stated
Long-term goals	×	No long-term goals stated
Measurable targets	×	No measureable targets
Transparent	?	No required reporting to the state, although GASB 31 requires local governments to disclose tax incentive costs in the notes to annual audits
Accountable		
Public analysis	×	Property Tax consequences ($30 million county property tax revenue foregone over 30 years can be inferred from careful reading of public disclosures
Expiration date	×	Permanent addition to County and Municipality IRB statutes.
Effective		
Fulfills stated purpose	×	No purpose stated
Passes "but for" test	?	
Efficient	?	
Key: ✓ Met × Not Met ? Unclear		

LG/al/sb