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FISCAL IMPACT REPORT

ORIGINAL DATE 1/28/2020

SPONSOR Papen LAST UPDATED _____ HB _____

SHORT TITLE Extend Agricultural Biomass Income Tax Credit SB 84

ANALYST Graeser

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY20	FY21	FY22	FY23	FY24		
	(\$890.0)	(\$890.0)	(\$1,770.0)	(\$1,770.0)	Recurring	General Fund (PIT & CIT)
			Construction Phase GRT See Fiscal Implications		Nonrecurring	General Fund (GRT)
			Construction Phase GRT See Fiscal Implications		Nonrecurring	Dexter
			Construction Phase GRT See Fiscal Implications		Nonrecurring	Chaves County

Parenthesis () indicate revenue decreases

Duplicates HB146

SOURCES OF INFORMATION

LFC Files

Responses Received From

New Mexico Department of Agriculture (NMDA)
 Energy, Minerals & Natural Resources (EMNRD)
 New Mexico Environment Department (NMED)

SUMMARY

Synopsis of Bill

Senate Bill 146 extends the Agricultural Biomass Income Tax and Corporate Income Tax Credit, Sections 7-2-18.26 and 7-2A-26 NMSA 1978, for ten years to January 1, 2030 and adds reporting requirements for both the taxpayer receiving the credit and the Taxation and Revenue Department (TRD).

SIGNIFICANT ISSUES

EMNRD notes the following significant issues:

The agricultural biomass tax credits allow a dairy or feedlot or their owners to claim a credit of \$5 per wet ton of agricultural biomass transported from the dairy or feedlot to a facility

that uses the biomass to generate electricity or create fuels. The tax credits were set to expire on January 1, 2020; SB84 would extend the credits until 2030.

The agricultural biomass tax credit has encouraged the development of this business opportunity in New Mexico. EMNRD issued certificates for 2 dairies in 2016 and 2017 for the transportation of 76,000 tons of wet manure to generate electricity. No applications were received by EMNRD in 2018 and 2019 as transportation operations were halted as the digester systems were upgraded. The upgrades have been completed and ready to begin transportation of the wet manure from the dairies.

SB84 adds a requirement that the taxpayer report the credit amount in a manner required by TRD. TRD must compile an annual report that includes the number of taxpayers approved to receive the credit, the aggregate amount of credits approved and any other information necessary to evaluate the credit. TRD must present the report to the Revenue Stabilization and Tax Policy interim committee and the Legislative Finance Committee with an analysis of the cost of the tax credit.

FISCAL IMPLICATIONS

Based on information provided by the only industrial participant in the program, current capacity of the Regenerative Thermal Oxidizer is about 177,000 tons of wet manure annually. At \$5 per ton, this equates to an annual credit claim of \$890 thousand. This is a fraction of the amount of manure produced annually by the dairy industry, the primary demanders of the biomass treatment processes. It is expected that one new plant of equivalent capacity will be built within the five-year estimating window and two more equivalent plants built in the fifth through tenth years of the credit.

The credit is capped annually at \$5 million with no rollover or queue provisions. This maximum is not shown in the table, although could be reached in the later years (FY27, FY28, FY29 or FY30) if the program is successful.

Somewhat offsetting the cost of the credit will be construction phase gross receipts taxes. The company developing the single current operating plant testifies that it has invested \$50 million in the state and has paid over \$2 million in gross receipts taxes (probably associated with the construction phase). The output of the plan is large volumes of methane, which can be burned in a natural gas turbine to produce electricity. If this generated electricity is used to power the digester and associated equipment, it is not gross receipts taxable, but if either the methane or the electrical power are sold, then those sales may be gross receipts taxable depending on the exact nature of the sale. Because of the uncertainty, we cannot quantify this offsetting potential gross receipts tax.

NMED's Ground Water Quality Bureau (GWQB) issues groundwater permits to dairies and other agricultural operations under the Water Quality Act tailored to the manure management practices of the individual facilities, including biomass to energy practices.

SIGNIFICANT ISSUES

NMED notes the following:

Agricultural biomass, as defined in the proposal, is wet manure and a by-product of dairy

and feedlot commercial operations. Wet manure from these agricultural operations is a significant source of methane emissions in New Mexico and the United States. Capturing and destroying this source of methane reduces the dangerous greenhouse gas released from dairies and feedlots and will help meet the Governor's mandates for reducing greenhouse gas emissions. This could fiscally benefit New Mexico's agricultural industry by reducing management costs associated with agricultural biomass.

Biocrude is a non-fossil fuel form of energy that can be used to produce electricity. Increased use of biocrude will reduce dependence upon fossil fuel fired electricity generation, thereby reducing toxic air pollutants that are emitted from conventional fossil fuels. Biofuels have emerged as one of the most strategically important alternative fuel sources and are considered an important way of limiting greenhouse gas emissions, improving air quality, and finding new energetic resources.

If implemented, SB84 will promote New Mexico's progress on meeting the requirements of the Governor's Executive Order on Climate Change and Waste Reduction (EO 2019-003), which requires the State of New Mexico to achieve a statewide reduction in greenhouse gas emission of at least 45 percent by 2030 as compared to 2005 levels, and to adopt approaches to reduce greenhouse gas and criteria pollutant emissions from light-duty vehicles.

EMNRD reiterates this analysis:

The agricultural biomass tax credits allow a dairy or feedlot or their owners to claim a credit of \$5 per wet ton of agricultural biomass transported from the dairy or feedlot to a facility that uses the biomass to generate electricity or create fuels. The tax credits were set to expire on January 1, 2020; SB84 would extend the credits until 2030.

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HB146 adds a requirement that the taxpayer report the credit amount in a manner required by TRD. TRD must compile an annual report that includes the number of taxpayers approved to receive the credit, the aggregate amount of credits approved and any other information necessary to evaluate the credit. TRD must present the report to the Revenue Stabilization and Tax Policy interim committee and the Legislative Finance Committee with an analysis of the cost of the tax credit.

And NMDA also contributes the following:

Agricultural biomass (manure) from dairies and feedlots is utilized by biomass facilities to generate electricity or gaseous fuel for commercial use. The transport of agricultural biomass to a facility is conducted on a dry/semidry basis and therefore costly to accomplish. The biomass tax credit is a critical incentive for a taxpayer of a dairy or feedlot to be an active component in this renewable energy sector. Without the tax credit the transportation of agricultural biomass from any reasonable distance becomes cost prohibitive. Redirecting agricultural biomass from a waste product to a renewable energy source is two-fold. It reduces the potential environmental footprint and also helps the renewable energy portfolio

goals of New Mexico.

PERFORMANCE IMPLICATIONS

If implemented, there may be performance implications for NMED. One of NMED’s current performance measures reported quarterly to LFC is the percent of days with a rating of good or moderate based on the air quality index (AQI). The AQI is an index of how healthy or unhealthy the air is on a daily basis in a certain area. If implemented, SB84 may improve overall air quality in the state and, thus, the percent of days rated good or moderate would increase, thereby improving the NMED performance measure.

EMNRD also reports on performance measures implications:

Extending the agricultural biomass tax credit aligns well with the Energy Transition Act (ETA), given the byproduct of the biomass is electricity produced from captured methane from a biodigester. This type of electricity is now considered a “Zero Carbon Resource” under the ETA and thus the tax credit assists in bringing these sources online.

Industry sources indicate that the annual capacity of the digester is as follows:

- 525,235 cubic yards of pack manure
- 177,030 tons
- Results in extracting 687,981,000 cubic feet of methane (renewable natural gas)
- Liquid digestate that come out the back end of the digester is a renewable organic fertilizer that has 95 percent less odor than raw manure when applied to crop fields.
- Both the methane and the fertilizer are valuable commodities that create value added in the state.

The provisions of this bill do create a tax expenditure. 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. However, a full analysis of the costs and benefits of this proposal, including monetizing an environmental positive externality, reducing carbon dioxide and methane emissions into the atmosphere, may warrant support of this proposal. In addition, there may be a largely unquantifiable GRT offset (see discussion at FISCAL IMPLICATIONS).

The LFC tax policy of accountability is met with the bill’s requirement to report annually to an interim legislative committee regarding the data compiled from the reports from taxpayers taking the deduction and other information to determine whether the deduction is meeting its purpose. Because both TRD and EMNRD have information on different aspects of this credit, an amendment on page 4 of the bill (Section J, reporting requirements) requiring both agencies to cooperate in preparing the report might be in order.

ADMINISTRATIVE IMPLICATIONS

TRD might have some difficulty properly administering credits transferred from the farmer or biomass conversion plant operator earning the credits to a presumably wealthy taxpayer buying the credits at a discount and applying the purchased credits to that taxpayer’s liabilities. In this case, the initial transfer will be from the operator of the plant to the out-of-state owners.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

SB84 is a duplicate of HB146. Last year's SB268 should be consulted for comparison.

TECHNICAL ISSUES

A feature of this tax credit is that the vouchers are transferable, and can be transferred to any entity that has New Mexico personal or corporate income tax liability. The credit is not refundable. Therefore, there is no problem here with the anti-donation clause. (NM Constitution, IX, Section 14.)

The only other NM tax credit that is transferrable is the Conservation Restriction Credit of 7-2-18.10 and 7-2A-8.9 NMSA 1978. From FY2011 through FY2015, 64,146 acres were entailed at a general fund cost of \$8,400,000 or about \$130 per acre. TRD calls this program a success. This agricultural biomass credit will result in a substantial amount of manure not entering the environment at a cost to the general fund of \$5 per ton of wet manure.

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL

NMED indicates the following:

New Mexico needs to encourage efforts that will help to meet the mandates of the Governor's Executive Order on Climate Change and Waste Reduction (EO 2019-003), which requires reductions of greenhouse gas emissions by at least 45 percent. The inclusion of agricultural sources of methane is an important opportunity to help achieve those reductions. The implementation of HB146 and new tax credits for agricultural biomass is a realistic starting point.

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

LFC Tax Expenditure Policy Principle	Met?	Comments
Vetted	?	This is second year of the proposal. The original bill was well vetted. Last year’s SB-268 was debated.
Targeted Clearly stated purpose Long-term goals Measurable targets	? ? ?	No explicit purpose, except the general to reduce the state’s carbon footprint. Industry sources have provided capacity estimates and a promise to expand. Industry sources have provided capacity estimates and a promise to expand.
Transparent	✓	Industry sources have provided accurate estimates of the future and the past.
Accountable Public analysis Expiration date	✗ ✓	Ten-year window.
Effective Fulfills stated purpose Passes “but for” test	✗ ?	Unknown. Expansion to new plants clearly depends on success of the first plant. This credit may well be essential to the economics of additional plants.
Efficient	?	This credit is attempting, at least in part, to monetize the positive environmental externality that creates a market failure.
Key: ✓ Met ✗ Not Met ? Unclear		

LG/al