BILL ANALYSIS AND FISCAL IMPACT REPORT
Taxation and Revenue Department

February 26, 2025

Bill: HB-548 **Sponsor:** Representatives Nathan P. Small and Meredith A. Dixon

Short Title: Oil & Gas Equalization Tax Act

Description: This bill enacts the Oil and Gas Equalization Tax Act. This act imposes a privilege tax on all products severed and sold at a rate of 0.85% of the taxable value of oil and on oil or other liquid hydrocarbons removed from natural gas at or near the wellhead. Information is included on how that value is to be determined using royalties paid or due, and situations where the value may be determined by the Taxation and Revenue Department (Tax & Rev), such as when the operator and purchaser are affiliated or the sale and purchase are not an arm's length transaction. A provision is included that this tax may not be levied more than once on the same product, and both an operator's report and a purchaser's report are required.

Effective Date: July 1, 2025

Taxation and Revenue Department Analyst: Lucinda Sydow and Sara Grubbs

Estimated Revenue Impact*					R or NR**	Fund(s) Affected
FY2025	FY2026	FY2027	FY2028	FY2029		
--	$394,100-$395,400	$421,300-$422,700	$437,400 - $438,800	$443,600 - $445,100	R	General Fund – New Oil & Gas Equalization Tax
--	($0 - $5,580)	($0 - $5,970)	($0 - $6,200)	($0 - $6,280)	R	Severance Tax Bonding Fund – Oil & Gas Severance Tax
--	($0 - $5,000)	($0 - $4,000)	($0 - $3,000)	($0 - $2,000)	R	Early Childhood Trust Fund– Oil & Gas Emergency School Tax
--	($0)	($0 - $1,000)	($0 - $2,000)	($0 - $3,000)	R	Severance Tax Permanent Fund– Oil & Gas Emergency School Tax
--	($0 - $255)	($0 - $270)	($0 - $320)	($0 - $325)	R	General Fund – Oil & Gas Conservation Tax
--	($0 - $30)	($0 - $32)	($0 - $78)	($0 - $79)	R	Oil and Gas Reclamation Fund – Oil & Gas Conservation Tax
--	($0 - $5,100)	($0 - $5,400)	($0 - $5,700)	($0 - $5,700)	R	Land Grant Permanent Fund – State Land Office Royalty Payments
--	($0 - $9,200)	($0 - $9,800)	($0 - $10,200)	($0 - $10,400)	R	Early Childhood Trust Fund– Federal Land Royalty Payments
--	($0 - Slightly negative)	($0 - Slightly negative)	($0 - Slightly negative)	($0 - Slightly negative)	R	Counties and School Districts (Ad Valorem Taxes)
--	($0 -	($0 -	($0 -	($0 -	R	General Fund – Gross

	Slightly negative)	Slightly negative)	Slightly negative)	Slightly negative)		Receipts Tax
--	($0 - Slightly negative)	($0 - Slightly negative)	($0 - Slightly negative)	($0 - Slightly negative)	R	Local Governments – Gross Receipts Tax

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

Methodology for Estimated Revenue Impact: [Section 3]: Tax & Rev used the December 2024 Consensus Revenue Estimating Group (CREG) forecast for oil production, prices and oil's taxable value to estimate the fiscal impact of the proposed 0.85% equalization tax. This new tax would increase revenue to the General Fund. Tax & Rev then estimated the potential loss of production associated with the tax that may offset revenues generated from various existing oil and gas taxes and their associated funds.

Tax & Rev assumes a potential 0.32% reduction in oil production based on a 2018 study from the American Economic Journal: Economic Policy on the effect of taxes and US oil production which found that increases in taxes can result in oil and gas production declines[1]. In this study, the authors estimated the after-tax price elasticity of oil supply is between 0.295 and 0.371. This means a 1% increase in taxes results in a 0.295% to 0.371% reduction in oil production. However, this study is based on oil production from California oil reservoirs. Every oil reservoir is unique, and as the author notes, oil production from hydraulic fracturing is more cost-effective, and may be less sensitive to changes in tax- in after-tax prices. As a result, Tax & Rev provides an estimated range for this fiscal impact. The potential loss in production would more likely to affect marginal oil producers.

The estimated reduction in production was then applied to the CREG's December 2024 forecast for oil. The distribution change to the various funds is based on the CREG's December 2024 forecast for oil and natural gas revenue and statutory distributions and includes impacts to taxes, including Gross Receipts Tax (GRT) and to state and federal royalties. Due to the uncertainty of an impact to production, Tax & Rev assumes the potential 0.32% drop represents the top of the range of potential loss of revenue to other state and local funds and the lower end of the range of new revenue from the proposed Equalization tax. The lower end of the range for other state and local funds revenues losses is equal to zero assuming no change in production. For the general fund revenue from the equalization tax this represents the top of the range.

Policy Issues: New Mexico currently levies six taxes on oil and gas. The following four taxes are based on the value of oil and gas severed from the soil and sold: Oil and Gas Severance Tax; Oil and Gas Conservation Tax; Oil and Gas Emergency School Tax; and Oil and Gas Ad Valorem Production Tax. In addition, New Mexico levies a Natural Gas Processors Tax on the value of products processed and an Oil and Gas Production Equipment Ad Valorem Tax on the assessed value of equipment used at production.

This proposal aligns with the four current taxes that are based on the value of oil severed from the soil and sold. The tax rates for all the taxes when the price of oil is over $18 a barrel, and the price of natural gas is over $1.35 per mcf, illustrate an overall lower effective rate for oil (8.27%) than for natural gas (8.97%), as demonstrated in the tables below. This lower effective tax rate on oil is driven by the difference in oil and natural gas tax rates for the Oil and Gas Emergency School Tax. The base oil rate is 3.15% and the base rate for natural gas is 4.00%. This proposal sets an "equalization" rate that is the difference of these two rates at 0.85%. Thus, this proposal aims to equalize the effective tax rates for the direct tax of oil and natural gas under the Oil and Gas Emergency School Tax and the new proposed Oil and Gas Equalization Tax.

[1] American Economic Journal: Economic Policy , November 2018, Vol. 10, No. 4 (November 2018), pp. 268-301

Taxes on Oil	Net Price of Oil ($/bbl)		
	Under $15	$15 to $18	Over $18
Oil and Gas Emergency School Tax	1.58%	2.36%	3.15%
Oil and Gas Severance Tax	1.88%	2.81%	3.75%
Subtotal	**3.46%**	**5.17%**	**6.90%**
Oil and Gas Conservation Tax	0.19% - 0.24%	0.19% - 0.24%	0.19% - 0.24%
Production Ad Valorem Tax	1.04%	1.04%	1.04%
Production Equipment Ad Valorem Tax	0.14%	0.14%	0.14%
Total	**4.83%**	**6.54%**	**8.27%**

Taxes on Natural Gas	Net Price of Natural Gas ($/mcf)		
	Under $1.15	$1.15 to $1.35	Over $1.35
Oil and Gas Emergency School Tax	2.00%	3.00%	4.00%
Oil and Gas Severance Tax	1.88%	2.81%	3.75%
Subtotal	**3.88%**	**5.81%**	**7.75%**
Oil and Gas Conservation Tax	0.19%	0.19%	0.19%
Production Ad Valorem Tax	0.88%	0.88%	0.88%
Production Equipment Ad Valorem Tax	0.15%	0.15%	0.15%
Total	**5.10%**	**7.03%**	**8.97%**
Natural Gas Processor's Tax			*depends*

Source: New Mexico Tax Overview Presentation, House Taxation and Revenue Committee, joint presentation by Tax & Rev and Legislative Finance Committee, January 29, 2025,
Note: ad valorem rates vary by year and taxing district. The rates presented here are statewide averages.

Sound tax policy considers not only the fiscal, economic and behavioral effects of a tax program, it also takes into account tax policy equity. Horizontal equity ensures the same statutes apply to all taxpayers, and vertical equity ensures the tax burden is based on taxpayers' ability to pay.

The state of New Mexico currently taxes natural gas producers at a rate that is higher than other products that are subject to severance taxes. This, in effect, erodes horizontal equity in severance taxes by offering one taxpayer a competitive advantage over another. By enacting this bill, horizontal equity will be proportionate between all taxpayers subject to the Oil and Gas Emergency School Tax and the new Oil and Gas Equalization Tax.

By creating the new 0.85% equalization tax rather than amending the Oil and Gas Emergency School Tax on oil to be 4.0%, the proposal directs the new revenue to the General Fund and not to the Severance Tax Permanent Fund (STPF), to the Early Childhood Education and Care Fund (ECECR), or to the Tax Stabilization Reserve (TSR) as current distributions statutes would dictate. Under current law, the amount of Oil and Gas Emergency School Tax that flows to the General Fund is capped at the amount received in FY2024, and excess revenue is diverted to the STPF, ECECR, or the TSR. These measures capping General Fund oil and gas revenue insulate the General Fund from volatility associated with oil and gas markets. This proposal will introduce volatility back into the recurring General Fund revenue forecast and increase the percentage of General Fund revenue dependent on oil-related revenue. As a matter of fiscal policy, New Mexico seeks to diversify its tax base, and increasing fiscal dependence on this source of revenue runs counter to that goal.

As an alternative to this proposal, rather than creating a new equalization tax, the bill could increase the oil and gas emergency school tax on oil from 3.15% to 4.00%, and then increase the FY2024 cap on general fund revenues by a commensurate amount.

Technical Issues: None.

Other Issues: [Section 11] The proposed advance payments language in this bill correctly mirrors Tax & Rev's proposed changes to oil and gas advanced payments included in HB-218. These changes streamline advanced payments to reflect the current process whereby Tax & Rev calculates the advanced payments and payments are collected annually, not monthly. The proposal will be consistent with advanced payments under the Oil and Gas Severance Tax, Oil and Gas Conservation Tax, Oil and Gas Emergency School Tax, and Oil and Gas Ad Valorem Production Tax if both bill proposals pass.

Administrative & Compliance Impact: This bill proposes the implementation of a new severance tax which mirrors current oil and gas severance taxes. Because the new equalization tax in on a tax base that is identical to the existing oil and gas severance taxes, implementation is fairly straightforward. Taxpayers already pay four taxes on a single form, and this new equalization tax can be added to that form. This means taxpayers will not face additional filing burden, and Tax & Rev will not need to register taxpayers for new tax accounts or accept additional returns.

Tax & Rev will update current oil and natural gas tax forms and publications to add this new tax and make changes to information systems. Implementation includes adding the new tax rate to the current combined rate on the existing oil and natural returns and forms which will ease the implementation for Tax & Rev and for taxpayers. Tax & Rev will test system changes and train employees on the administration of the proposed tax.

This bill will have a low impact on Tax & Rev's Information Technology Division (ITD) of approximately 200 hours or just over one month and $46,000 of contractual costs.

Tax & Rev's Revenue Processing Division (RPD) will add the new tax program to MAVRO, RPD's remittance processing system.

Estimated Additional Operating Budget Impact*				R or NR**	Fund(s) or Agency Affected
FY2025	FY2026	FY2027	3 Year Total Cost		
$46.0	--	--	$46.0	NR	ITD – Contractual Costs
$8	$8	--	$16	NR	RPD – MAVRO implementation

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

Related Bills: Relates to HB-218, Sections: 120,124,132, and 141