MINUTES
of the
FIRST MEETING
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

June 19, 2017
State Capitol, Room 307
Santa Fe

The first meeting of the Revenue Stabilization and Tax Policy Committee for the 2017 interim was called to order by Senator Carlos R. Cisneros, chair, on Monday, June 19, 2017, at 10:09 a.m. in Room 307 of the State Capitol in Santa Fe.

Present
Sen. Carlos R. Cisneros, Chair
Rep. Jim R. Trujillo, Vice Chair
Rep. Sharon Clahchischilliage
Rep. Roberto "Bobby" J. Gonzales
Rep. Tim D. Lewis
Rep. Javier Martínez
Sen. Clemente Sanchez
Sen. William E. Sharer
Rep. James R.J. Strickler
Rep. Carl Trujillo
Sen. James P. White

Absent
Rep. Jason C. Harper
Sen. Gay G. Kernan
Rep. Antonio Maestas
Sen. Mark Moores
Sen. George K. Munoz
Sen. John Arthur Smith
Sen. Peter Wirth

Designees
Rep. Daymon Ely (attending as guest)
Rep. Rod Montoya
Sen. Nancy Rodriguez
Rep. Patricia Roybal Caballero
Sen. Elizabeth "Liz" Stefanics

Rep. David E. Adkins
Rep. Eliseo Lee Alcon
Rep. Cathrynn N. Brown
Sen. William F. Burt
Sen. Jacob R. Candelaria
Rep. Bealquin Bill Gomez
Rep. Bill McCamley
Rep. Debbie A. Rodella
Rep. Angelica Rubio
Rep. Patricio Ruiloba
Rep. Tomás E. Salazar
Rep. Larry R. Scott
Rep. Nathan P. Small
Rep. Candie G. Sweetser
Sen. Bill Tallman
Sen. Pat Woods

Staff
Pam Stokes, Staff Attorney, Legislative Council Service (LCS)
Ric Gaudet, Researcher, LCS
Tessa Ryan, Staff Attorney, LCS

Guests

The guest list is in the meeting file.

Handouts

Handouts and other written testimony are in the meeting file.

Monday, June 19

Post-Session Fiscal Review

David Abbey, director, Legislative Finance Committee (LFC), and Dawn Iglesias, economist, LFC, updated the committee on key aspects of the state's finances. Mr. Abbey noted that information in the handout accompanying the presentation was updated after the special session. He continued as follows.

Post-session summary. In the past year, the legislature has, in effect, gone through three special sessions to overcome the state's challenging fiscal circumstances. In the 2017 regular session, measures passed by the legislature would have brought revenue and spending levels into balance, but subsequent action by the governor required that a special session be held to address the vetoes that upset that balance and the vetoes of higher education and legislative branch appropriations. Legislation enacted in the recent special session left the fiscal year (FY) 2017 estimated reserves balance at $166.4 million and that for FY 2018 at $23 million.

Also of note: 1) FY 2018 appropriations are all virtually flat, with the exception of those for the judicial branch, which, overall, are 2.5% higher than in the previous fiscal year; 2) the period between FY 2008 and FY 2018, despite being marked by population growth and the expansion of Medicaid, could be seen as the "lost decade" for its lack of net change in appropriation levels; and 3) the legislature's efforts at enacting measures to raise additional revenue were blocked by the governor.

All told, the estimated recurring spending for FY 2017 exceeds the estimated recurring revenue for that year by over $480 million; for FY 2018, that figure is $150.4 million. Those imbalances have been reconciled through solvency measures. The situation calls for a conversation on generating sustainable revenues.

Year-to-date revenues. Ms. Iglesias continued the presentation, first by noting that the recently released revenue tracking report distributed to the committee provides more detail on the information she would cover.

Some of the key measures influencing revenue levels are employment growth, active rig counts, oil production and the prices of oil and natural gas. In the area of employment, year-over-year growth of .46% is tracking closely with the December 2016 Consensus Revenue Estimating Group (CREG) estimate. Much of that growth is in the private sector and, specifically, in the construction industry. Meanwhile, in the area of energy extraction, the number of active rigs is increasing, and oil production is exceeding expectations. Oil and natural gas prices are on par with the December 2016 CREG forecast for FY 2017, but they are below the forecast for FY 2018. That deviation is attributed to the fact that oil inventories are not depleting as expected.

Elsewhere, there are signs of strength in General Fund revenues. For the period between February and April, those revenues were higher than in the same period last year. Much of that increase is attributed to strength in gross receipts tax (GRT) and severance tax revenues. Through April, FY 2017 revenues were tracking higher than forecasted. Ms. Iglesias noted that improving the CREG's access to data from the Taxation and Revenue Department (TRD) related to tax credits would help the group better understand the causes of that strength.

A graph on page 13 of the handout shows, for the 18-month period before April, the differences between actual revenue levels and forecasted revenue levels.

Mr. Abbey indicated that a new revenue estimate would become available in August and that he is generally confident it will reveal revenue levels higher than forecasted. He underscored the LFC's concern, as it affects revenue forecasting, about the inadequacy of data shared by the TRD. He continued the presentation as follows.

FY 2019 fiscal outlook and state government condition. It is projected that recurring revenue will not return to its FY 2015 level until FY 2019; that is, next year will most likely bring more fiscal challenges. As shown in the table on page 16 of the handout, future fiscal years show recurring revenue gaps of over $150 million.

In the area of state employment, almost 3,000 jobs have been cut since FY 2009, and there are high annual turnover and vacancy rates, particularly in occupations whose members work on the front lines of health and safety. Much of that turnover and vacancy is attributed to the state's failure to compensate at levels on par with the market.

In the area of pension funds, the Public Employees Retirement Association's (PERA's) unfunded actuarial accrued liability as of June 30, 2016 is over $4.8 billion. For the Educational Retirement Board (ERB), that figure is over $6.6 billion. For the past several years, the agencies have overestimated investment returns; that prompted the ERB to lower its investment return assumption from 7.75% to 7.25%.

Meanwhile, legal challenges to the state's state equalization guarantee, public school capital outlay, food stamps processing, developmental disabilities programs and early childhood funding policies threaten the state's fiscal soundness.

Proposed joint meeting with LFC; tax reform comparison chart. Mr. Abbey invited the committee to consider conducting a joint meeting with the LFC in Farmington in July.

Mr. Abbey and Ms. Iglesias then turned the committee's attention to a chart in the handout that compares several aspects of three key tax reform bills recently introduced. Mr. Abbey noted that the LFC scrambled to put together a fiscal impact report (FIR) for House Bill 8 from the special session once LFC staff saw it, which was not until after the bill was introduced. Since then, staff have analyzed the bill more thoroughly and produced the FIR that was distributed to the committee. Ms. Iglesias reviewed details of the chart, which highlights data in the FIR.

Questions and Discussion

On questioning, the presenters and committee members addressed the following topics.

Energy prices and production. Concerning energy prices and production, Mr. Abbey explained that domestic oil inventories have not diminished, despite OPEC's curtailing of oil production, in part because technological advancements have revolutionized extraction techniques, which, in turn, has dramatically increased production. He added that: 1) revenue estimators generally subtract $2.00 to $3.00 from the West Texas Intermediate price of oil per barrel when estimating the price of oil in New Mexico; and 2) the $48.00-per-barrel projection for FY 2018 is, in hindsight, probably a bit too high.

Responding to another member's question, a committee member described the situation in San Juan County, as it relates to energy extraction, as follows: 1) one company, which has plans to spend many millions of dollars on big projects, is waiting for the issuance of 50 permits before it can move forward on the projects; 2) impending transitions in management at the federal level will help expedite those issuances; and 3) thousands of energy sector jobs have recently been lost, which has resulted in the departure of thousands of people from the region. Another member remarked that: 1) federal and state environmental and regulatory agencies, by implementing policies adverse to nonrenewable energy production industries, play a bigger role in tax policy than realized; and 2) the policies pursued by those entities — and the state's financial needs — are at odds with each other but should be reconciled.

Revenue estimates; General Fund reserves. Mr. Abbey and Ms. Iglesias clarified points related to the General Fund financial summary as follows: 1) generally, the summary's figures are based on estimates, while the General Fund revenue tracking report's figures are based on actuals; 2) the 2.7% reserves figure presented in the summary reflects the approximately $100 million in revenue raised through solvency measures taken during the regular and special sessions; 3) the effects of having potentially overestimated the price of oil for FY 2018 could be offset by strength in gross receipts and other aspects of the economy; 4) although the growth in the health and social services sector is leveling off, the sector is nevertheless a key factor promoting growth in GRT revenues; and 5) improvement in the construction sector has also boosted those revenues.

On the subject of revenue and spending, members commented that: 1) even though the revenue picture is brightening, the state is still far from a 10% reserves level; 2) lawmakers shortchanged the state when they cut personal income tax rates and removed the GRT from food; and 3) lawmakers need to work on ensuring that revenues stabilize.

Growth and contraction in state government and in revenue and spending. A member remarked that the information presented on state government job cuts revealed only part of the picture, which includes the fact that, in the years shortly before those cuts, state government had swelled in size. The member suggested that the state grew too rapidly and requested that, in future presentations on the topic, a more complete picture of growth and contraction be provided. Mr. Abbey recognized that there were years in the past decade of extraordinary growth made possible by spikes in energy prices. In hindsight, he said, revenue estimates for those years were too high.

Tax compliance. A member stressed the need for more enforcement of taxes and cited examples of laxness in enforcing tax laws. Mr. Abbey responded that the LFC issued a lengthy report last October on tax audit and compliance, which focused on the "tax gap", or difference between tax obligations and collections. He recommended that the committee consider adding the report as an item to its agenda, and he recommended that the TRD be requested to testify on its response to the report.

Public school facilities funding. Mr. Abbey expressed hope that strides made in public school facilities funding would compel a court to dismiss any active lawsuit related to alleged deficiencies in that funding. He added that the Public School Capital Outlay Oversight Task Force would take up the topic this interim.

Reliability of data from TRD; tax expenditures. A member expressed doubt about the reliability of data from the TRD. Mr. Abbey said that the accuracy of data is not at issue, but rather the need for better reporting from the TRD on tax credits. He described the state's having had problems with unforeseen, large-scale claims and the lingering possibility of a recurrence of those problems. The member stressed the need for the state to evaluate its tax expenditures and that it, while careful to not drive business out of the state, eliminate those that do not yield their intended results.

Amazon's collection of GRT. Mr. Abbey and Ms. Iglesias clarified that: 1) Amazon has been collecting the state, not local, portion of the GRT since April 1, in spite of its technological capacity to collect both; 2) monthly revenue from that source is about $2 million to 3 million; 3)

Amazon is not collecting the tax on sales for which it serves as a platform, which constitute about one-half of all of its sales; and 4) recent legislation attempted to capture that revenue.

Pension agencies. Mr. Abbey noted that the LFC puts out quarterly investment reports that feature updates on returns of the pension agencies' funds. He highlighted some of the content of those reports, including: 1) comparisons between the PERA's and ERB's performance with comparable funds; and 2) amounts paid for active management of the funds, management which, in the PERA's case, has not in the past decade yielded above-average returns. Lastly, Mr. Abbey remarked that the agencies focus more on their investment strategies than on their fund liabilities and benefits structures.

Requests for information; topics for future discussion. LFC and committee staff agreed to: 1) send a member county-level detail on GRT growth in the construction sector; and 2) send the committee electronic links to the most recent tax expenditure report and to the LFC-produced quarterly investment report.

Members suggested the following topics for future meetings: 1) updates on federal health care legislation and its effects on state revenues; 2) updates on the health of the oil and gas industries; and 3) GRT imposition and collection for internet-based sales.

Work Plan and Meeting Schedule

Ms. Stokes reviewed the committee's 2017 proposed work plan and meeting schedule. Concerning Item 4 on the work plan, she gave an update on the LCS's efforts to select a contractor to conduct a tax study on the gross receipts and other tax bases in the state. Members commented on that topic as follows.

- The study should be objective, in that it not recommend policy. Furthermore, the goal of any policy pursued in response to the study should: 1) simplify the tax system; 2) raise revenue to a level adequate for the state to meet its obligations; and 3) attract new business to the state.

- Any policy pursued in response to the study should incorporate a strategy for upholding existing bond repayment obligations tied to GRT revenue streams.

The committee adopted the proposed work plan and meeting schedule.

Adjournment

There being no further business before the committee, the committee adjourned at 11:58 a.m.