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FISCAL IMPACT REPORT

ORIGINAL DATE 2/18/07
 LAST UPDATED 2/26/07 HB 666/aHENRC/aHFL#1

SPONSOR Silva

SHORT TITLE Electric Power Plant Property Valuation SB _____

ANALYST Francis

REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Non-Rec	Fund Affected
FY07	FY08	FY09		
	* See Narrative			

(Parenthesis () Indicate Revenue Decreases)

Similar SB874

Relates to HB665, SB340

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY07	FY08	FY09	3 Year Total Cost	Recurring or Non-Rec	Fund Affected
Total		\$65.0	\$65.0	\$130.0	Recurring	TRD

(Parenthesis () Indicate Expenditure Decreases)

SOURCES OF INFORMATION

LFC Files

Taxation and Revenue Department

Response Received from:

Taxation and Revenue Department (TRD)

SUMMARY

Synopsis of House Floor Amendment #1

An amendment on the House Floor removes the requirement that the Taxation and Revenue Department (TRD) specify the information required to support a claim of obsolescence and the requirement for TRD to give sufficient time for a taxpayer to establish a claim before TRD issues its valuation. TRD still must provide reasons for its denial of a claim of obsolescence.

Synopsis of HENRC Amendment

The House Energy and Natural Resources Committee amended House Bill 666 in the following ways:

- Changed the title to more accurately reflect the content of the bill
- Inserted an emergency clause to make the legislation effective upon signing
- Deletes a section on allowing alternative valuation methods that was proposed in the original
- Adds a new section that allows alternative valuation methods if the Taxation and Revenue Department disputes a claim for functional or economic obsolescence.

Synopsis of Original Bill

House Bill 666 modifies the valuation methodology for property used in the generation, distribution or transmission of electricity. The valuation can include deductions for “functional” and “economic” obsolescence.

- Economic obsolescence is defined as the loss of value caused by unfavorable economic influences or factors outside of the property not including physical depreciation.
- Functional obsolescence is loss due to functional inadequacies or deficiencies caused by factors within the property not including physical depreciation.

The taxpayer choosing to include economic and/or functional obsolescence must submit a claim documenting the obsolescence. Such documentation may include industry comparisons, volume reductions, and other objective evidence of obsolescence. The Taxation and Revenue Department (TRD) will determine if the evidence is sufficient and notify the taxpayer if a claim is rejected with the reasons and what additional information is needed to establish obsolescence, giving a taxpayer enough time to comply.

This section removed by HENRC amendment:

A taxpayer is given a choice of valuation methods:

1. capitalization of income
2. market value of stock
3. cost less allowance for obsolescence and depreciation.

Whichever method chosen the taxpayer must use that method for subsequent years unless, after three years, the taxpayer can show sufficient cause to change methods.

This act is applicable to property tax years 2007 forward.

HENRC amendment declares an emergency.

FISCAL IMPLICATIONS

The amendment allows the choice of valuation for cases where TRD disputes the claims of functional or economic obsolescence. While there is no precise way to determine the impact of this modification to the valuation methodology, since there is a choice of methods in cases where obsolescence is in dispute, property valuations could change using the alternative methods. TRD

reports changes in valuation are likely to be minor. If assessed values do decrease as a result of this change, the impact depends on what the affected county requires from property tax collections. If the county requires the revenue prior to this change in valuation, rates for all property taxpayers will rise or fall to compensate for the change in valuation. The county could keep the rates the same and the impact would come from tax collections.

TRD has provided an illustration of what would happen if the valuation were down 8 percent due to the HENRC amendment. It estimates a decline of \$2.5 million in property valuation statewide. The county that would see the largest is San Juan followed by Bernalillo and Dona Ana (Table).

Illustration: Potential Fiscal Impacts of Proposed Legislation (continued)

County	Estimated Loss in Assessed Value	% of Total Assessed	Estimated Loss/Shift in	Total Obligations	Percent of Total Obligations
San Juan	29,196,833	0.8	700,293	95,615,186	0.73
Bernalillo	9,981,643	0.1	419,683	435,271,076	0.1
Dona Anna	7,491,161	0.3	234,209	75,519,474	0.31
McKinley	6,075,899	1	211,577	20,850,187	1.01
Lea	4,213,000	0.2	114,839	64,538,371	0.18
Sandoval	2,849,264	0.2	82,931	55,906,362	0.15
Eddy	3,634,123	0.2	71,523	48,170,687	0.15
Santa Fe	2,688,325	0.1	68,904	104,907,897	0.07
Hidalgo	3,169,771	2.7	68,780	2,674,582	2.57
Chaves	2,147,058	0.3	56,775	20,865,164	0.27
Luna	2,326,718	0.7	50,689	7,546,152	0.67
Otero	1,687,133	0.2	48,830	18,018,686	0.27
Rio Arriba	1,903,442	0.1	43,083	40,314,249	0.11
Roosevelt	1,741,853	0.8	36,681	5,487,214	0.67
Valencia	1,155,562	0.1	35,330	22,818,557	0.15
Curry	1,520,663	0.3	34,017	11,458,201	0.3
Torrance	1,145,581	0.5	27,542	6,156,077	0.45
Taos	1,357,724	0.2	25,721	13,443,901	0.19
Lincoln	842,621	0.1	22,194	16,633,893	0.13
Socorro	691,757	0.4	20,804	5,398,415	0.39
Cibola	639,243	0.3	20,253	6,941,814	0.29
San Miguel	627,867	0.2	18,302	9,696,950	0.19
Grant	833,581	0.2	17,687	10,706,591	0.17
Sierra	675,198	0.3	16,461	4,756,414	0.35
Quay	582,404	0.5	15,487	2,895,108	0.53
Guadalupe	433,341	0.5	14,413	2,975,485	0.48
Catron	1,109,953	1.4	14,269	1,202,547	1.19
Colfax	547,955	0.1	13,690	11,589,882	0.12
Union	533,473	0.5	12,027	2,457,270	0.49
DeBaca	374,763	1	9,327	1,052,933	0.89
Mora	204,282	0.3	5,396	1,658,522	0.33
Harding	65,788	0.2	1,383	695,182	0.2
Los Alamos	5,896	0	123	12,021,752	0
Totals	92,453,872		2,533,224	1,140,244,782	

*8% of Total Electric

** Estimated loss in assessed value multiplied by weighted average nonresidential property tax rate.

Source: TRD

The oil and gas industry has experienced problems with claims of functional and economic obsolescence. House bill 665, a similar bill for that industry, only defines these concepts in statute. This bill goes an additional step for the electric industry and allows for an alternative valuation. To the extent that the electric industry has had claims denied, the alternative valuation methods would likely lead to either increased litigation or lower valuations.

ADMINISTRATIVE ISSUES

TRD:

The Department has performed several unitary valuations on properties of the type listed in the proposal due to specific characteristics of the associated properties. The proposal, as amended, would require approximately five additional unitary appraisals annually. One FTE with salary and benefits totaling approximately \$65,000 would be required to accomplish this task.

OTHER ISSUES

TRD:

Unitary Assessment, Functional and Economic Obsolescence

The unit rule of appraisal is defined as "...an appraisal of an integrated property as a whole without reference to the value of its component parts. The approach is based on a view that informed buyers and sellers purchase or sell a viable operating unit, rather than portions of the property. This procedure incorporates "going concern" value associated with a customer base, as opposed to a new customer base a firm would need to develop if it purchased only portions of an established business. The unit rule may be applied appraisals based on the cost approach, comparable sales approach or income approach.

As indicated above, the cost approach to appraisal estimates market value by making a series of adjustments to estimates of replacement cost, including allowances for economic and functional obsolescence. The sales comparison approach essentially appraises property by comparing the property to prices of similar properties that have recently sold – with appropriate adjustments. The income approach estimates the amount of money a typical purchaser would pay for a (typically income-producing) property based on the income generating ability of the property.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

HB 666 relates to HB665 and SB340 as far as proposing to use functional and economic obsolescence as a factor for valuation. SB 874 is similar to HB 666 as amended and a duplicate of the original.

NF/mt