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

SPONSOR Taylor **ORIGINAL DATE** 2/14/07 **LAST UPDATED** 3/15/07 **HB**

SHORT TITLE Oil & Gas Property Alternative Unit Valuation **SB** 340/aSFC/aHTRC

ANALYST Francis

REVENUE (dollars in thousands)

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

(Parenthesis ( ) Indicate Revenue Decreases)

Duplicates HB 665

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY07	FY08	FY09	3 Year Total Cost	Recurring or Non-Rec	Fund Affected
Total		(232.0) *See Narrative	(232.0)	(464.0)	Recurring	Taxation and Revenue Dept.

(Parenthesis ( ) Indicate Expenditure Decreases)

Duplicates HB 665 as amended

SOURCES OF INFORMATION
LFC Files

Responses Received From
Energy Minerals and Natural Resources (EMNR)
Taxation and Revenue Department (TRD)

SUMMARY

Synopsis of HTRC Amendment

The House Taxation and Revenue Committee amended Senate Bill 340 to changes a provision relating to those properties regulated by the Federal Energy Regulatory Commission. In the original bill, the due date for supplements to the annual report with claims of obsolescence are due no later than April 15 of the tax year following the year in which the property was subject to valuation. This amendment changes this due date to April 15th of the tax year.

Synopsis of SFC Amendment

The Senate Finance Committee amended Senate Bill 340 to redefine the deadlines for the Taxation and Revenue Department (TRD) to give notice of deficiency. TRD must provide notice by April 1 or 30 days after the return is filed but no later than April 15th. If the property is regulated by the Federal Energy Regulatory Commission (FERC), notice shall be provided within 15 days of the filing of the FERC report and the taxpayer shall have 10 days to respond.

The SFC amendment also clarifies the title and makes the first applicable tax year as beginning on or after January 1, 2008.

Synopsis of Original Bill

Senate Bill 340 was introduced for the interim Revenue Stabilization and Tax Policy Committee. The New Mexico Oil and Gas Association (NMOGA) requested RSTP's endorsement on this bill. The bill amends the Property Tax Act, allowing the valuation of pipelines, tanks, sales meters and plants used in the processing, gathering, transmission, storage, measurement or distribution of oil, natural gas, carbon dioxide or liquid hydrocarbons to be reduced upon a showing of "functional obsolescence" or "economic obsolescence." These two concepts are added to the definition of "other justifiable factors."

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

The amendment requires the taxpayer to claim and document the economic or functional obsolescence. If the Taxation and Revenue Department (TRD) disagrees it must notify the taxpayer of the TRD determination in writing setting forth the reasons for its determination and specifying the supporting information that TRD requires.

FISCAL IMPLICATIONS

The fiscal impact of this change is uncertain. If these clarifications allow for more claims of economic and functional obsolescence, then assessed property values will decline by the amount of the claims. According to the New Mexico Oil and Gas Association (NMOGA), there have not been more or less claims but rather many of those claims that have been rejected are being litigated. Their position is that TRD began rejecting valid claims of obsolescence and therefore artificially inflating the assessed value. If the change lowers the amount of litigation, there may be a net savings for the TRD operational budget.

NMOGA:

By defining functional and economic obsolescence it should clarify that obsolescence is separate and apart from "physical depreciation" and currently allowed in both statute and regulation. While the Property Tax Division has allowed "physical depreciation", it has been ignoring "other justifiable factors" which is functional & economic obsolescence and contends that obsolescence is part of physical depreciation.

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:

Due to the HENRC amendments, fiscal impacts of the proposed legislation are expected to be minor, but uncertain because: 1) the number of taxpayers, assessed values and locations of affected properties affected by the proposal are unknown at the moment, and 2) if the proposal results in decreased assessments for some taxpayers, the tax rate setting process would cause some tax rates to adjust upward, offsetting most of the revenue impacts. Thus, the bill would not generally reduce revenue but could result in a shift of the tax burden from properties affected by the legislation to all other taxpayers. The Department's rough estimate of the extent of tax shifting or loss to property tax recipients primarily counties, municipalities and school districts – is on the order of several hundred thousand dollars annually.

SIGNIFICANT ISSUES

As reported in 2006 session for HB375-S:

The New Mexico Oil and Gas Association have indicated that this legislation clarifies the intent of the current statute. According to NMOGA, the intent embodied in the phrase "any other justifiable factor" includes economic and functional obsolescence. NMOGA feels that this obsolescence was generally accepted from 1973 till 2003 when the Property Tax Division of the Taxation and Revenue Department began rejecting claims of obsolescence without adequate explanation to the taxpayers.

In the statute, there are already references to functional and economic obsolescence which is clarified in the regulations as follows:

(c) For purposes of Subsection B of Section 7-36-27 NMSA 1978, "other justifiable factors" includes, but is not limited to, functional and economic obsolescence.

(i) Functional obsolescence is the loss in value due to functional inadequacies or deficiencies caused by factors within the property.

(ii) Economic obsolescence is the loss in value caused by unfavorable economic influences or factors outside the property.

(iii) Requests for economic or functional obsolescence must be made at the time the annual report is filed. The request must be supported with sufficient documentation, and must be based on a situation present at least six (6) months prior to January 1 of the tax year. An economic or functional obsolescence factor must be provided together with documentation to support and demonstrate how the factor was arrived at. Such documentation shall consist of objective evidence demonstrating functional or economic obsolescence such as comparisons to a documented industry standard, to a close competitor or to an engineer's or appraiser's valuation, or any other comparable objective evidence of functional or economic obsolescence. Failure to provide documentation or proof satisfactory to the director will result in denial of an obsolescence adjustment. (http://www.tax.state.nm.us/regs/Property_Tax_Code.pdf page 36-65)

POSSIBLE QUESTIONS

Functional and economic obsolescence are already referenced in the statutes. What does this bill do that changes those references?

NF/mt