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

ORIGINAL DATE 01/25/12
SPONSOR SFC **LAST UPDATED** 02/15/12 **HB**

SHORT TITLE Locomotive Fuel Gross Receipts **SB** 45/SFCS

ANALYST Walker-Moran

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY12	**FY13**	**FY14**	**FY15**	**FY16**		
	$0.0	($3,332.2)*	($3,487.6)	$(3,581.3)	Recurring	General Fund
	$0.0	($328.1)*	($343.4)	($352.6)	Recurring	Municipal Equivalent Distribution
	$0.0	($457.5)*	($478.8)	($491.8)	Recurring	Small County Assistance Fund
	$0.0	($457.5)*	($478.8)	($491.8)	Recurring	Small City Assistance Fund

(Parenthesis ( ) Indicate Revenue Decreases)

Duplicates HB 47 substitute

SOURCES OF INFORMATION

LFC Files

Responses Received From
Economic Development Department (EDD)
Taxation and Revenue Department (TRD)
Joint analysis with Department of Finance and Administration (DFA)

SUMMARY

Synopsis of Senate Finance Committee Substitute Bill

The Law currently provides a deduction from the gross receipts tax (GRT) and compensating tax for locomotive fuel beginning on July 1, 2013, contingent on certification by economic development Department that the construction of a railroad locomotive refueling facility project in Dona Ana County has commenced by July 1, 2012.

Senate Bill 45 amends section 7-9-110.3 NMSA 1978 to provide a deduction from gross receipts tax (GRT) and compensating tax for locomotive fuel beginning July 1, 2013, provided that the EDD certifies to the TRD that at least one common carrier, prior to July 1, 2012, in a class A county with a population according to the most recent federal decennial census of more than 200,000 but less than 300,000 has commenced land acquisition, acquisition of all necessary permits, and actual construction.

The purpose of the deduction on fuel loaded or used in a locomotive engine from gross receipts and from compensating tax is to encourage construction, renovation, maintenance and operation of railroad locomotive refueling facilities and related activities in New Mexico.

On or after July 1, 2012, SB 45 amends the qualifying capital investment to $50 million or more in railroad infrastructure improvement, including railroad facilities, track, signals and supporting railroad network, located in New Mexico, provided that the new railroad infrastructure improvements are not required by a regulatory agency to correct problems identified by that agency as requiring necessary corrective action. For one year, eligibility for the deduction is still limited to a railroad that after July 1, 2011 made a qualifying capital investment of $100 million or more in new construction or renovations at the railroad locomotive refueling facility in which the fuel is loaded.

The bill also describes the purpose and requirements of the locomotive fuel deduction, such that the Economic Development Department (EDD) can measure the effects of the deduction. EDD is required to compile an annual report containing information on those who claim the deduction, the number of jobs created as a result of the deduction, and the amount of the tax expenditure. This report is to be used to evaluate the effectiveness of the deduction.

The existing law has a contingent effective date of July 1, 2013 which is repealed in this bill.

The effective date of the bill is July 1, 2012. There is no sunset date. The LFC recommends adding a sunset date.

FISCAL IMPLICATIONS

This bill may be counter to the LFC tax policy principle of adequacy. According to the LFC staff General Fund Recurring Appropriation Outlook for FY14 and FY15, December 2011 forecasted revenues will be insufficient to cover growing recurring appropriations.

This estimate was made using information from the Surface Transportation Board including fuel use, fuel costs, and track miles operated for Class I railroads operating in New Mexico. Data on diesel price forecasts from the U.S. Energy Information Administration (EIA) was also used.

* The new $50 million investment requirement might allow Union Pacific to qualify for this deduction sooner than it otherwise would have. In this case, the revenue impact would be much larger for FY2014.

Policy Issues: The GRT deduction for railroad fuel was adopted by the 2011 legislature in order to encourage development of a new railroad re-fueling facility in southern New Mexico. The proposal would lower the new investment requirements for this GRT deduction, meaning that there would be a smaller “bang for the buck” in added economic development as a result.

A possible goal of this bill may be to further stimulate the railroad industry in New Mexico. By reducing fuel costs this bill would make it slightly more profitable for railroads to operate in New Mexico. However, the bill would also add complexity and narrow the gross receipts and compensating tax base. An argument in favor of the proposal is that it would treat similar business activity the same.

Estimated Revenue Impact – Detailed Discussion: On the immediate horizon, only one major rail operator, BNSF Railway, will likely qualify for this within the next fiscal year. As such, data were taken from BNSF's Class I Railroad Annual Report for 2010 submitted to the Surface Transportation Board and available through STB's website. According to this report, BNSF operates 32,378 total miles of track in the US, of which 1357 miles (or 4.19 percent) are in New Mexico. Also from that report, BNSF's system-wide expenditure on locomotive fuels was approximately $2.785 billion.

Data on historic and forecasted diesel prices were then taken from the U.S. Energy Information Administration's Annual Energy Outlook 2012 Early Release. These data were converted to growth rates for calendar years 2010 through 2016. Applying these growth rates to BNSF's 2010 expenditure yielded an estimated system-wide expenditure on locomotive fuel across relevant years.

This analysis used the ratio of track operated in New Mexico relative to the entire system as a proxy for percentage of fuel use, but it is likely that track operated in NM by BNSF accounts for fewer actual ton-miles than a more heavily trafficked stretch of track. This analysis assumes that NM track is 65 percent as trafficked on average, resulting in an estimate that BNSF's use of fuel in NM accounts for 2.72 percent of its system-wide use. Applying this percentage (2.72 percent) to total expenditure gives an approximation of the value that would be subject to the compensating tax in New Mexico. The compensating tax rate of 5.125 percent is taken against that total to calculate a total revenue impact, which is further divided between the statutory distributions.

The $50 million investment necessary for the deduction must occur after July 1, 2012. This analysis assumes that BNSF will meet this threshold prior to the effective date of the legislation. The analysis also recognizes that other railway operators could eventually reach the $50 million threshold. In that case, the actual fiscal impact in the out years would be larger than this estimate suggests.

Compensating tax was deemed the appropriate revenue stream to use in these calculations. Given the estimated expenditure of BNSF on fuel, the approximate two percent difference between gross receipts tax at its fueling facility in Belen and the compensating tax is not insignificant. The analysis assumes, therefore, that BNSF has strong incentive to structure its fuel purchases in such a way that they would pay compensating tax rather than GRT. This assumption may not hold for smaller railway operators.

PERFORMANCE IMPLICATIONS

The LFC tax policy of accountability is met with the bill's requirement that the EDD and TRD report annually to the interim Revenue Stabilization and Tax Policy 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.

Per EDD, expanding the types of investments that allow a company to qualify for the deduction, thereby allowing a company to qualify for the deduction without creating new jobs, will keep the Department and other economic development organizations from using the deduction to attract other investments to the state. The original legislation requires the Department to report on the number of jobs created by the deduction and the return on the state's investment in the deduction. That report will reflect that fewer jobs were created as a result of the deduction if businesses that do not create new jobs qualify for the credit. The bill will have a serious negative impact on job creation and render the deduction largely useless as a job-creation tool.

ADMINISTRATIVE IMPLICATIONS

This bill has minimal impact on the Taxation and Revenue Department. Taxpayer and employee education will be required.

OTHER SUBSTANTIVE ISSUES

The Railroad Revitalization and Regulatory Reform Act of 1976 might provide railway operators an avenue to pursue recourse against inequitable tax treatment. Although the 4R Act has historically been used to challenge treatment across transportation industries, it could provide grounds to challenge intra-industry discriminatory practices. If it did, amending the original statute through the legislative process to apply this deduction more equitably might be less costly to the state than litigation.

ALTERNATIVES

Per EDD, the deduction as originally enacted is an effective incentive. It attracted Union Pacific to New Mexico. Union Pacific is now constructing a $400 million + refueling facility in Santa Teresa, which will create 3,000 construction jobs and more than 600 permanent jobs.

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

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