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

ORIGINAL DATE 02/14/13
SPONSOR SFC **LAST UPDATED** 03/11/13 **HB**

SHORT TITLE Algae & Geothermal Energy Equipment Valuation **SB** 387/SFCS

ANALYST Smith

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY13	FY14	FY15	FY16	FY17		
Small	Small	Small	Small	Small*	Recurring	Property Tax

(Parenthesis ( ) Indicate Revenue Decreases)
*TRD states initial impact is small but could become considerable as the industry develops.

SOURCES OF INFORMATION
LFC Files

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

SUMMARY

Synopsis of Bill

The Senate Finance Committee substitute for Bill 387 (SB 387) creates a new section of Chapter 7, Article 36 NMSA 1978 (Property Tax Code) regarding the method of valuation for algae and geothermal generation equipment used for generation, transmission, or distribution of electric power or energy subject to valuation for property taxation purposes. SB 387 provides that for taxable years beginning on or after January 1, 2014 through December 31, 2028, the Taxation and Revenue Department (TRD) shall determine the actual cost of construction of the algae or geothermal generation equipment. The TRD shall then reduce the actual cost of construction by the amount of the federal investment tax credit claimed, if any, associated with the purchase of the algae or geothermal equipment. The TRD shall reduce this amount by depreciation using a twenty-fold useful life and for any other justifiable factors. The value for tax purposes shall be 20 percent of this amount. As such, the algae and geothermal energy equipment will be valued at an amount which is 20 percent of actual cost of construction reduced by federal investment tax credit and 20-year, straight-line depreciation.

SB 387 defines algae generation equipment as cultivation, harvesting, and conversion equipment and systems and related equipment used to generate electricity out of algae biomass. It defines geothermal generation equipment as heat exchangers, turbines, and associated electrical generating equipment and related equipment used to generate electricity from geothermal energy, cooling towers, wells, pumps, gathering systems, and related tangible and intangible drilling costs incurred to produce, distribute, or use energy from a geothermal deposit.

Lastly the TRD is required to compile a report for the review of the Revenue Stabilization and Tax Policy committee.

Effective Date: Not specified; 90 days following adjournment

FISCAL IMPLICATIONS

The TRD notes that the current impact is small because the Property Tax Division (PTD) does not have any algae or geothermal plants and equipment on the rolls. However, these could develop into significant technologies and therefore represent considerable lost revenue in the foreseeable future.

This bill may be counter to the Legislative Finance Committee (LFC) tax policy principle of adequacy, efficiency and equity. Due to the increasing cost of tax expenditures revenues may be insufficient to cover growing recurring appropriations.

Estimating the cost of tax expenditures is difficult. Confidentiality requirements surrounding certain taxpayer information create uncertainty, and analysts must frequently interpret third-party data sources. The statutory criteria for a tax expenditure may be ambiguous, further complicating the initial cost estimate of the expenditure's fiscal impact. Once a tax expenditure has been approved, information constraints continue to create challenges in tracking the real costs (and benefits) of tax expenditures.

SIGNIFICANT ISSUES

The TRD notes that the twenty-year useful life of the project has no specific foundation and should be made subject to determination based on utility treatment of this kind of generation equipment for tax purposes, particularly as relates to the (likely) more durable geothermal capital equipment components. It should be explicitly noted that combining the two types of generation capital investment seems somewhat arbitrary, as they are very different technologies and may have very different equipment associated and associated useful life. Algae is still early in its development as a sustainable method of energy generation while geothermal has been around much longer.

The valuation procedure outlined in this legislation conflicts with Section 7-36-29(C)(3) which states that the determination of value for property taxation purposes shall not be less than twenty percent of the tangible property cost of the electric plant.

The twenty-year depreciation schedule is at odds with class life (reciprocal of annual depreciation schedules) represented by industry as well as conventional class life used on renewable electrical generation equipment by the IRS. Those are typically twenty-five or thirty years.

The TRD recognizes other justifiable factors including the typical twenty-year term of power purchase agreements in determining obsolescence and class life.

The twenty-year class life stipulation in this legislation is at odds with the twenty-five year sustainability opinion required for the Production Tax Credits.

PERFORMANCE IMPLICATIONS

The LFC tax policy of accountability is met since the TRD is not required in the bill to report annually to an interim legislative 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.

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

SS:EWM/svb:blm