FISCAL IMPACT REPORT

SPONSOR Ferrary/Sedillo Lopez/Johnson/Pinto/Thomson

LAST UPDATED 2/13/23
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SHORT TITLE Liquor Tax Rates and Differentials

BILL NUMBER House Bill 230

ANALYST Faubion

APPROPRIATION*
(dollars in thousands)

Appropriation		Recurring or Nonrecurring	Fund Affected
FY23	FY24		
--	$200.0	Nonrecurring	General Fund

Parentheses ( ) indicate expenditure decreases.
*Amounts reflect most recent version of this legislation.

REVENUE*
(dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY23	FY24	FY25	FY26	FY27		
	($25,080.0)	($25,300.0)	($25,560.0)	($25,780.0)	Recurring	General Fund
	$2,000.0	$1,890.0	$1,740.0	$1,630.0	Recurring	Local DWI Grant Fund
	$270.0	$270.0	$270.0	$270.0	Recurring	Class A Muni
	$570.0	$560.0	$540.0	$530.0	Recurring	Drug Court Fund
	$178,210.0	$178,870.0	$179,470.0	$180,110.0	Recurring	Alcohol Harms Alleviation Fund

Parenthesis ( ) indicate revenue decreases
*Amounts reflect most recent version of this legislation.

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT*
(dollars in thousands)

	FY23	FY24	FY25	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
	--	$316.4	$316.4	$632.8	Recurring	HSD
	$164.5	---	-	$164.5	Recurring	TRD
Total	$164.5	$316.4	$316.4	$797.3		

Parentheses ( ) indicate expenditure decreases.
*Amounts reflect most recent version of this legislation.

Conflicts with SB61, SB220, and HB321
Duplicates SB259

Sources of Information

LFC Files

Responses Received From
Department of Health (DOH)
Department of Finance and Administration (DFA)
Human Services Department (HSD)
Early Childhood Education and Care Department (ECECD)
Regulation and Licensing Department (RLD)
Public Education Department (PED)
Taxation and Revenue Department (TRD)

SUMMARY

Synopsis of House Bill 230

House Bill 230 increases liquor excise tax rates to 25 cents per serving, indexes the rates to inflation, and distributes a portion of the revenue from the tax to a new alcohol harms alleviation fund.

Under the proposed bill, the distributions of the net receipts attributable to the liquor excise tax are as follows:

Percent Distribution of Liquor Excise Tax Revenue	Earmarked Use
12%	Local DWI Grant Fund
0.25%	Municipalities in a class A county with a population of 30,000 – 60,000
1.5%	Drug Court Fund
86.25%	Alcohol harms alleviation fund

House Bill 230 appropriates $200 thousand from the general fund to the Department of Finance and Administration in FY24 to contract for services and coordinate proposals to the Legislature for the expenditure of funds in the alcohol harms alleviation fund. Any unexpended funds remaining at the end of fiscal year 2024 shall revert to the general fund.

The effective date of this bill is July 1, 2023.

FISCAL IMPLICATIONS

The general fund would no longer receive any revenue from liquor excise tax net receipts versus approximately 49.5 percent under current statute, resulting in a negative general fund revenue impact of $25.1 million to $25.8 million through the forecast period. The proposed excise tax rates are much higher than the current rates. When LFC applied the new rates to historical collections, the amount collected would be approximately four to five times higher under the proposed rates than current rates, in aggregate.

The amount to be distributed to municipalities that are located in a class A county with a population of more than 30 thousand but less than 60 thousand is amended to 0.25 percent of net receipts instead of the $20,750 monthly in current law. The change of this distribution from a fixed rate to a percentage has a small impact on that distribution given the projected revenues. Currently, only Farmington qualifies for this distribution. If only one municipality qualifies for this distribution, as has been the case recently and is assumed in this fiscal analysis, that city will receive $270 thousand more each year.

The amount distributed to the local DWI grant fund and the drug court fund would increase slightly, by $2 million and $570 thousand, respectively, due to the increase in the excise tax rate.

The new alcohol harms alleviation fund would receive the largest distribution at 86.25 percent, resulting in approximately $178 million to $180 million in revenue through the forecast period.

The bill does not include a recurring appropriation but does create the alcohol harms alleviation fund. The fund allows for continuing appropriations, donations, investment interest, and other sources and is subject to appropriation by the Legislature to the Human Services Department, Department of Health, Early Childhood Education and Care Department, Public Education Department, and Higher Education Department. The revenue distributions contained in this bill are a recurring expense to the general fund. Any unexpended or unencumbered balances remaining at the end of the fiscal year shall not revert to the general fund. LFC has concerns with including continuing distribution language in the statutory provisions for newly created funds because earmarking reduces the ability of the Legislature to establish spending priorities.

House Bill 230 appropriates $200 thousand from the general fund to the Department of Finance and Administration in FY24 to contract for services and coordinate proposals to the Legislature for the expenditure of funds in the alcohol harms alleviation fund. Any unexpended funds from this appropriation remaining at the end of fiscal year 2024 shall revert to the general fund.

TRD notes the following regarding their methodology for determining the fiscal impact:

> The Taxation and Revenue Department (TRD) used the Liquor Excise Tax forecast from the Consensus Revenue Estimating Group (CREG) in December 2022 to estimate the revenue impact of the proposed tax increases and distribution changes. The Liquor Excise Tax covers a variety of products. The bill proposes tax increases to all the categories based on new rates at a serving size volume versus the wholesale volume taxed today. TRD converted the new rates to current volumes to measure the price increases. TRD applied different demand elasticities to the products. Based on a study of the impact of price and income elasticities of demand for Alcoholic Beverages by Ornstein and Levy, they found beer to have a price elasticity of -0.3 and for distilled spirits, an elasticity of -1.5. Based on these elasticities, beer consumption is less sensitive to price changes versus distilled spirits. Their study found inclusive evidence of elasticity impacts for wine consumption. TRD assumed the same price elasticity for wine, fortified wine cider, micro brewed beer as for beer. The price increases per product are extremely large, thus the application of price elasticity is difficult to model. The drop in liquor consumption could be higher than what is modeled, reducing positive revenue impacts forecasted to the various funds. Also, if the purchase of liquor products for consumption moves to neighboring states or to online purchasing (see *Significant Issues* below), then the assumed drop in liquor purchases in state could also be higher still. The study by Ornstein and Levy also notes no strong evidence of substitutable products for either beer,

wine or distilled spirits. TRD makes no assumption of changes in consumption patterns between liquor products. A note that the proposed liquor rate indexing for inflation starts in FY28, beyond the fiscal impact horizon.
For the fiscal impact among different funds, TRD applied the new distribution percentages proposed in 7-1-6.40 NMSA 1978.

SIGNIFICANT ISSUES

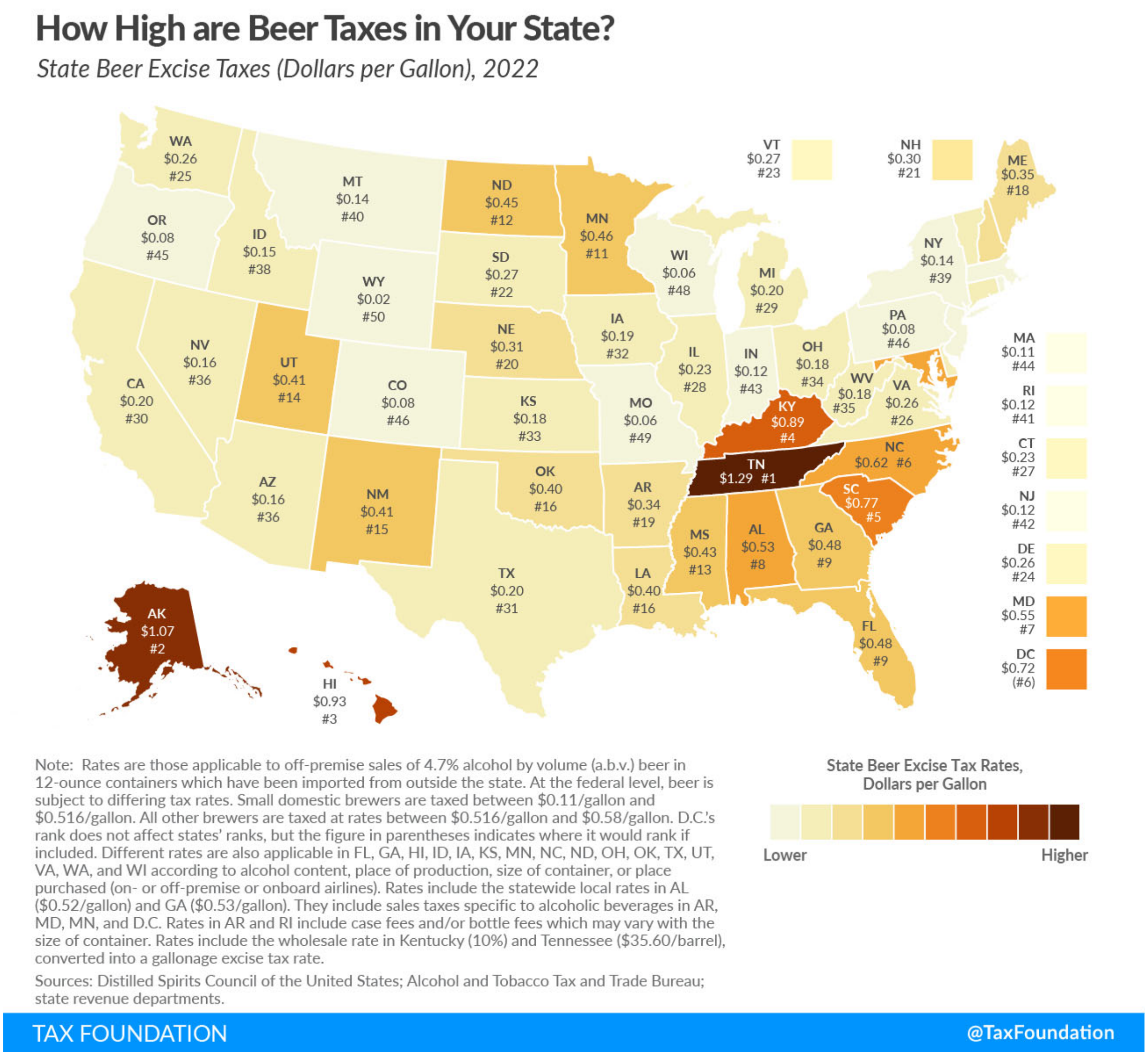
TRD notes the following:

Alcohol and substance abuse are among the costliest health problems in the United States. Different studies have shown that public investment reduces alcohol and substance abuse and delays abuse initiation at young ages. In that regard, the redistribution of revenue to targeted alcohol abuse funds may impact and support community programs. This would establish a consistent future fund balance for budgeting appropriations from these funds but would permanently divert gross receipts revenue from the general fund.

New Mexico's tax code is out of line with most states in that complex distributions are made through the tax code instead of through appropriations. As an alternate to this proposal and revenue earmarks, the liquor excise tax could continue to be distributed to the general fund and alcohol abuse funding needs could be provided for through general fund appropriations in HB2. The more complex the tax code's distributions, the costlier it is for TRD to maintain the GenTax system and the more risk is involved in programming changes.

The change to a tax rate by consumption serving size volume versus the wholesaler volume (see *Technical Issues*) adds complexity to the tax code and increases the tax compliance burden on both taxpayers and TRD. Complexity does not comport generally with the best tax policy. On the other hand, removing the rate differentials for micro-brewed beer and cider and wine produced by small winegrowers, will simplify the tax code for liquor.

The rate increases by liquor product are substantial, approximately 250 percent for spirituous liquors, 275 percent for wine, and 550 percent for beer and cider. The increases will be passed on to consumers, which may drive some of the purchasing of products to neighboring states with lower tax rates or to online retail purchasing. The map below from the Tax Foundation compares the tax rates of beer between states. Currently among neighboring states, New Mexico along with Utah, have the highest tax rate on beer per gallon. The proposed tax increase to beer, will place New Mexico the highest in the nation.



Studies are mixed on the impact of raising prices to reduce liquor consumption. Part of the inclusive correlation is due to various other factors that are used to curb consumption of alcohol as it relates to health outcomes and preventing impaired driving. In empirical studies it is hard to control for other social and legal steps that are taken to curb excessive drinking and then driving. Finally, there are studies pointing to the differences in policies and the impact by gender and race. If increasing liquor rates is part of a social effort to curb excessive drinking to improve quality of health and prevent impaired driving, then a comprehensive approach to tax policy, health and social policy would be recommended.

The Department of Health (DOH) notes the following:

According to data from the New Mexico Department of Health's Bureau of Vital Records and Health statistics, 2,273 New Mexicans died from alcohol-related causes in 2021. This means that approximately 1 in 11 deaths in New Mexico were due to alcohol-related causes. The age-adjusted death rate per 100 thousand New Mexican residents for alcohol-related causes increased from 65.7 deaths in 2017 to 102.8 deaths in 2021.

According to the latest cost estimates produced by CDC, excessive drinking cost New Mexico $2.2 billion in 2010, which equates to $1,084 per person. Most of these costs were due to the impact of binge drinking. Jason Blanchette *et al.'s* study found that most of the cost associated with alcohol's harms are borne by those who don't drink excessively or who don't drink at all. These alcohol-related harms include violence, and motor vehicle injuries.

Increasing alcohol taxes, according to the Centers for Disease Control and Prevention's (CDC) Community Guide and the World Health Organization's (WHO) SAFER initiate are proven methods to reduce excessive alcohol consumption.

Alexandra Wright *et al.'s* 2017 review found a significant inverse relationship between alcohol taxes or prices and the consumption of alcohol products (i.e., higher prices lead to less alcohol consumption); a relationship which held for both light and heavy drinking behaviors. However, Rebecca Ramirez *et al.*'s review found that even modest tax increases in Illinois and Maryland were associated with decrease in excessive consumption and alcohol-related problems.

Brian Vandenburg *et al.*'s 2016 study found that alcohol taxes can be slightly regressive. William Kerr *et al.* found that some consumers may choose to purchase alcohol beverages in bulk at discount rates to offset increases in price. Jürgen Rehm *et al.'s* 2022 review found that unrecorded consumption was driven more by: 1) the availability and type of unrecorded alcohol; 2) whether such consumption was non-stigmatized; 3) the primary population groups which consumed unrecorded alcohol before the policy change; and 4) the policy measures taken compared to the direct result of tax increases.

Alexandra Wright and *et al.'s* 2017 review found that the associated revenue streams may be subject to a significant degree of volatility. The volatility around tax revenue stems from different consumer behaviors. Tax revenues could decrease as long-term habits are gradually changed or increase over time as consumers become more accustomed to higher prices. However, Jason Blanchette *et al.'s* 2019 study found that all taxes on alcohol account for only one tenth of alcohol-related costs.

According to New Mexico Behavioral Risk Factor Surveillance Survey (NM BRFSS), 46 percent of New Mexico adults in 2021 drank alcohol within the past month. NM BRFSS also reports that in 2021, 14.6 percent of New Mexicans engaged in binge drinking (which is 4 or more alcoholic drinks on occasion for women and 5 or more alcoholic drinks on occasion for men).

The Department of Finance and Administration notes the following:

Raising taxes on alcohol is an evidence-based strategy that public health policy analysts have studied and much of the research states that raising alcohol taxes will reduce consumption. "Higher alcohol taxes are consistently related to lower total alcohol consumption, and there is very strong evidence for the effectiveness of alcohol taxes in targeting heavy drinkers and excessive alcohol use (Guindon et all 2022)."

One of the main reasons for the increase in liquor excise tax is to reduce consumption. Some public health experts state for every 1 percent increase in alcohol cost, drinking will decrease by:

.30 percent in beer consumption,
.60 percent in wine consumption, and
.64 percent in liquor consumption.

Reducing the consumption of liquor and reducing the harms related to alcohol misuse is a significant issue in New Mexico. The proposed .25 cent per drink LET tax rates will increase the current LET tax by 257.14 percent. and may decrease consumption of alcohol by 9.98 percent according to a report prepared by Healthy Places Consulting for the LHHS committee on March 31, 2015.

The Human Services Department (HSD) notes the following:

The burden of substance use disorder among the New Mexico population is well documented with regard to drug and alcohol injury and death. New Mexico continues to rank at or near the top of the nation with both alcohol and drug overdose death. The drug overdose death rate in New Mexico has doubled in the last five years increasing from 24.6 deaths per 100 thousand population in 2017 to 50.6 deaths per 100 thousand population in 2021 (NMDOH Bureau of Vital Records and Health Statistics). Additional funding to support services for substance use disorder could help decrease substance related deaths and injuries.

Per a 2016 report prepared by Kitty Richards, MPH, total costs associated with excessive alcohol consumption in New Mexico in 2010 were $2,233 million per year. Of total costs, $332.7 (14.9 percent) million was spent on health care. Of 2010 health care costs, 44 percent were paid for through Medicaid ($77.65 million) and state and local governments ($68.54 million), totaling $146.19 million (Sacks, et al. 2015).

Total costs of excessive alcohol consumption	2,232.9
Health care costs of excessive alcohol consumption	332.7
Health care costs of excessive alcohol consumption covered by Medicaid, state, and local government	146.19
Health care costs of excessive alcohol consumption covered by state and local government only	68.54
Health care costs of excessive alcohol consumption covered by Medicaid only	77.65

Based on an annual growth rate of 5 percent per year in Medicaid expenditures from 2010 through 2015 (Henry J. Kaiser Family Foundation, Urban Institute and KCMU analysis of CMS Form 64 data, FY 1990-2014), a projected $99 million in Medicaid dollars were spent to treat and care for illnesses caused by excessive alcohol consumption in New Mexico in 2015. The estimated share of Medicaid expenditures borne by the state and Federal government were $21.81 million and $77.33 million, respectively.

Health care costs of excessive alcohol consumption covered by Medicaid only	99.14
Medicaid health care costs of excessive alcohol consumption covered by state government	21.81
Medicaid health care costs of excessive alcohol consumption covered by Federal government	77.33

A 2015 reported prepared by Dr. David Jernigan, Dr. Lisa Marie Cacari Stone, and Dr. Victoria Sanchez titled *The Economic and health Effects of a Twenty-Five Cents per Drink Alcohol Excise Tax Increase in New Mexico* found that increasing taxes on alcohol has been found to decrease overall alcohol consumption and improve health outcomes related to overconsumption of alcohol. It also reduces deaths due to alcohol. It stated:

- A 25 cent per drink increase in New Mexico's alcohol excise tax would result in an additional $187.2 million in total cost savings for New Mexico's economy. It would also result in a 9.98 percent decrease in alcohol consumption.
- This decreased consumption would save 52 lives, prevent 306 violent acts, and prevent 12,375 cases of alcohol dependence or abuse in New Mexico every year.
- The decrease in alcohol consumption would also result in an annual increase in economic productivity of $128.1 million in New Mexico.
- Productivity gains would more than offset job losses in the alcohol industry. The additional state revenues generated from the increased alcohol excise tax would create 616 jobs in the health and mental health care fields (if the additional revenues were directed toward health care) or 2,898 jobs if the funds simply went into the state's general fund (Center on Alcohol Marketing and Youth, 2015).
- Underage drinking - alcohol use among New Mexicans between the ages of 12 and 20 – would decrease by 13 percent (7,150 youth). Binge drinking among youth would decrease by 4,680 people. The annual costs of underage drinking would be reduced by $20.6 million.
- Excessive drinkers, who make up 18.9 percent of adults age 18 and above, will pay the overwhelming bulk (75 percent) of the tax, an average of $51.14 in additional tax per year, compared to $9.85 for non-excessive drinkers (32.1 percent of adults). Non-drinkers (who comprise 49 percent of adult New Mexicans) will pay nothing. (Center on Alcohol Marketing and Youth, 2015).
- Case studies from other states that have raised alcohol excise taxes suggest that states do not lose alcohol sales to neighboring states because of increased alcohol excise taxes, particularly if, like New Mexico, they have thriving tourism markets and gaming establishments and are sparsely populated along borders (Nesbit, 2005).

ADMINISTRATIVE IMPLICATIONS

TRD will conduct staff training, update forms, instructions, and publications. TRD will also need to produce communications to impacted taxpayers, including specifications of the proposed changes to tax rates. Starting in FY27 for new rates in FY28, TRD will need to annually update forms, instructions and publications to reflect the change in indexed liquor excise tax rates. These will be incorporated into annual tax implementation which is not covered in the budget timeline below.

TRD's Information Technology Division (ITD) estimates that the changes would incur approximately 750 hours or about five months of development with contractual hours for a cost of $157,500. TRD's Administrative Services Division (ASD) will have 60 hours of staff workload between 2 full-time equivalent (FTE) staff, with effort related to testing new distributions and reports in the GenTax system. TRD's Revenue Processing Division (RPD) will also devote staff workload to test the new liquor rates for the initial change and in FY28 for the new indexed rates. RPD staff will also require more time devoted to taxpayer inquiries and customer service to answer questions on the new rate structures.

Adding all new rates with an effective date for July 1, 2023, does not allow TRD enough time to update changes to forms, instructions, GenTax, the tax system of record, and Taxpayer Access Point (TAP), the taxpayer interface system. It is recommended to add an effective date of January 1, 2024, to properly implement these rate changes.

DFA notes HB230 appropriates $200 thousand to DFA to contract for services to coordinate proposals to the Legislature for the expenditures in the alcohol harms alleviation fund, but the bill does not appropriate any funding for the agency to perform these additional duties.

HSD notes there is no appropriation to HSD designated in HB230, however the bill stipulates that HSD could request to have an appropriation of the alcohol harms alleviation fund through the Legislature. A program that could be proposed using the distribution outlined in HB230 would require additional 2 FTE and a portion of two supervisors' time to implement. BHSD will need to develop a process for ensuring appropriate and rigorous evaluation of the efficacy and impact of this appropriation. It could require 2 FTE calculated at a 70 pay band and .2 FTE of two supervisors calculated at a 75 pay band. The total funding required for this staff time would be $241 thousand for salaries, fringe benefits and operating costs. In addition, this project would require an evaluation budget of approximately $75 thousand. This would allow HSD to provide meaningful data to the LFC and other stakeholders about the effectiveness of this allocation.

Possible HSD outcome measures for programs funded under HB230 could include:

- Decrease in alcohol and drug use,
- Decrease in psychiatric symptoms,
- Decrease in family conflict,
- Decrease in in legal issues,
- Increase in employment,
- Decrease in medical symptoms.

HSD notes that it is unclear whether this funding can be matched with Federal Medicaid funds. The best possible Federal Medicaid matching would be at 50 percent (the Administrative rate). However, obtaining this match is questionable, because grant funding programs need federal approval in order to receive federal matching funds. If a county operated a substance abuse center at an annual cost to the benefit of Medicaid members, then Federal matching of state funds is possible. If approved, then HSD could get matching funds, either at the 50 percent Administrative rate, or the Regular FMAP, depending on if the program is service-based.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

HB230 conflicts with SB61, SB220, and HB321 which change the liquor tax rate and/or the liquor tax revenue distributions.

HB230 duplicates SB259.

TECHNICAL ISSUES

HSD notes the preferred term is "substance use disorder" rather than "substance abuse."

TRD notes the following technical issues:

> The entire range of liquor products are receiving a tax increase by taxing smaller quantities of volume. The liquor excise tax is imposed on the wholesaler who sells the products at the current referenced volumes in statute. Using the current 7-17-5(4) which is the charge on fortified wine as an example, the tax rate is $1.50 per liter. A liter has 33.81 fluid ounces. Extrapolating the new rates to the 1 liter, the rate is now $2.42 per liter. TRD recommends that instead of taxing by the smaller quantities, to increase the tax by the current volume measure to allow for a smoother implementation of these tax rates and to be consistent with tax rates and reporting that taxpayers are familiar with. Taxing amounts by ounce adds complexity for the taxpayer and TRD, which is contrary to the tax policy of simplicity.
>
> TRD notes that there is no language to prevent the tax rate from declining should the adjustment for the consumer price index result in a lower rate, i.e. if there is deflation rather than inflation. If the intention is to only increase rates, TRD suggests the following language to be added on page 5, line 21, "after whole cent, except if the result would be a rate less than the rate for the preceding fiscal year,".
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> TRD notes that under current law many new alcoholic products do not meet definitions under the statute; therefore, it is unclear what rate should be applied to them. For example, premade alcoholic mixed drinks, alcoholic seltzers, and alcoholic mead to do not cleanly fall in the current definitions. TRD suggests defining broader categories that will anticipate the vast variety of alcoholic beverages that become marketable.

OTHER SUBSTANTIVE ISSUES

DOH notes the following:

> In 2021, the age-adjusted death rate per 100 thousand New Mexican residents who died from alcohol-related causes was nearly double that for males (146.5) compared to females (60.9) according New Mexico's Indicator Based Information System (NM-IBIS). Nearly 3 in 4 (73 percent, or 1655 individuals) of the alcohol-related deaths occurred in New Mexicans aged 25-64 years old, making alcohol the leading cause of death in this age group. American Indians bore the highest burden of alcohol-related deaths with a death rate of 311.1 deaths per 100 thousand residents during 2021. McKinley County (335.7 deaths per 100 thousand), Cibola County (179.8 deaths per 100 thousand), and Rio Arriba County (176.6 deaths per 100 thousand) had the highest age-adjusted death rates

for alcohol-related causes during 2021. Whereas the counties of Roosevelt (52.7 deaths per 100 thousand) and Los Alamos (35.2 deaths per 100 thousand) had the lowest age-adjusted rate for alcohol-related deaths during 2021.

Meenakshi Subbaraman *et al.* (2020) found that effects of beverage-specific tax increases decreased drinking volume and alcohol-related consequences differently for different gender and racial groups. Higher beer tax was significantly associated with lower odds of any drinking among white women, while for African American women it led to a lower amount of beer and total alcohol consumed. Higher spirits tax was significantly associated with both lower beer and total volume among Hispanic women and men as well as decreased amount of wine consumed by Hispanic women.

ALTERNATIVES

TRD notes sub-section 1.B proposes to change the Farmington flat amount carve out to a percentage-based amount. There is a Local Liquor Excise Tax, Section 7-24-10 NMSA 1978, which has similar legislative prescribed uses, that perhaps could be expanded to permit Farmington to enact this tax, rather than adding additional complexity to the tax code.

DFA notes the Behavioral Health Collaborative (BHC), created in statute in 2004, consists of 15 state agencies that provide oversight and services for New Mexico citizens to include behavioral health, substance abuse and mental health services, including each of the agencies cited in this bill. The bill lists five purposes for this fund and each of them align with goals of the BHC, perhaps the BHC may have a mechanism in place to coordinate proposals to the legislature for the expenditures from the new alcohol harms alleviation fund.

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.

JF/al/ne/rl/al