

Revenues in New Mexico: The Five Year Path to a Revenue Squeeze

Executive Summary

State revenue grew by nearly 50 percent between FY 2003 and FY 2008. This healthy growth, however, is linked to a disturbing trend: a greater reliance on unstable revenue sources and a lesser reliance on stable sources.

Personal income taxes are considered a stable revenue source. They can be expected to grow in proportion to any growth in wages and population. Severance taxes – that is, taxes collected on the oil and natural gas extracted from New Mexico's public lands – are a less stable revenue source. The amount we collect in severance taxes fluctuates greatly over time, as it is tied to prevailing prices rather than production output. As the price of gasoline and natural gas rose, beginning in 2003, our state revenues grew. But those prices stabilized during FY 2007 and are expected to remain flat in 2008.

During the FY 2003-2006 timeframe, the state Legislature also enacted cuts to personal income and capital gains taxes, as well as eliminated sales tax on food to be consumed at home. The top marginal rate for the personal income tax was cut from 8.3% to 4.9%, or nearly in half. The personal

income and capital gains tax cuts will result in a \$400 million loss in revenue in FY 2008. Due to a combination of state and federal actions, the revenue from the estate tax was cut to zero between FY 2003 and FY 2006.

The result of these changes in revenue sources was that oil and gas revenues came to represent a larger share of the state's economy. As a larger share, they have a larger overall impact when they decline or flatten due to falling or stagnant oil and gas prices. This increases the level of risk to the stability of the state's general fund.

New Mexico's revenue growth rate has already slowed significantly. Growth was 1.2% in FY 2007 and is expected to be 3% in FY 2008. With the state's population growth estimated at 1.1% annually, and inflation at 3% annually, revenue growth has to be at least 4% in order for the state to maintain its current level of services.

Given the current revenue projections, the state will just barely be able to maintain current services, and increases will be out of the question.