

REVENUE WE CAN RELY ON

**DIVERSIFYING OUR STATE REVENUE IS CRITICAL
FOR EQUITABLY FUNDING OUR FUTURE**

By Paige Knight, MPP
October 2021



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In order to provide the opportunities necessary for our children to thrive both now and into the future, New Mexico needs to ensure we have revenue that is adequate, sustainable, and equitable.

But due to past tax cuts that favored the wealthy and well-connected, combined with our over-dependence on volatile oil and gas revenues, our ability to continually invest in the programs and services that help families build a brighter future – like quality public education, child care assistance for working parents, economic development initiatives, and behavioral health services – is at risk.

With sustainable state revenues, we can build a stronger, more prosperous New Mexico. Here are the top five reasons New Mexico needs to focus on diversifying our revenue streams now, and recommendations on where we can begin.

1. WE ARE DANGEROUSLY DEPENDENT ON THE BOOM-AND- BUST CYCLE OF THE OIL AND GAS INDUSTRY

Our state budget remains overly reliant on revenues from the oil and gas industry. In fiscal year (FY) 2021, about 30% of our state revenues were attributable to oil and gas activity.¹ The industry's inherent volatility makes it difficult for New Mexico to meet the budget needs of our schools, hospitals, courts, and more on a consistent basis (see Figure I, page 3). When market cycles that are out of our control result in a drop in oil and gas prices and production – and therefore a drop in state revenue – lawmakers often choose to make cuts to our state budget and the programs and services that families rely on rather than raise revenue elsewhere.

New Mexico's revenues are ranked the fourth most volatile in the nation by Pew Trusts, with Figure II (page 4) clearly demonstrating in grey the ups and downs of our oil and gas revenues, known as severance taxes.²

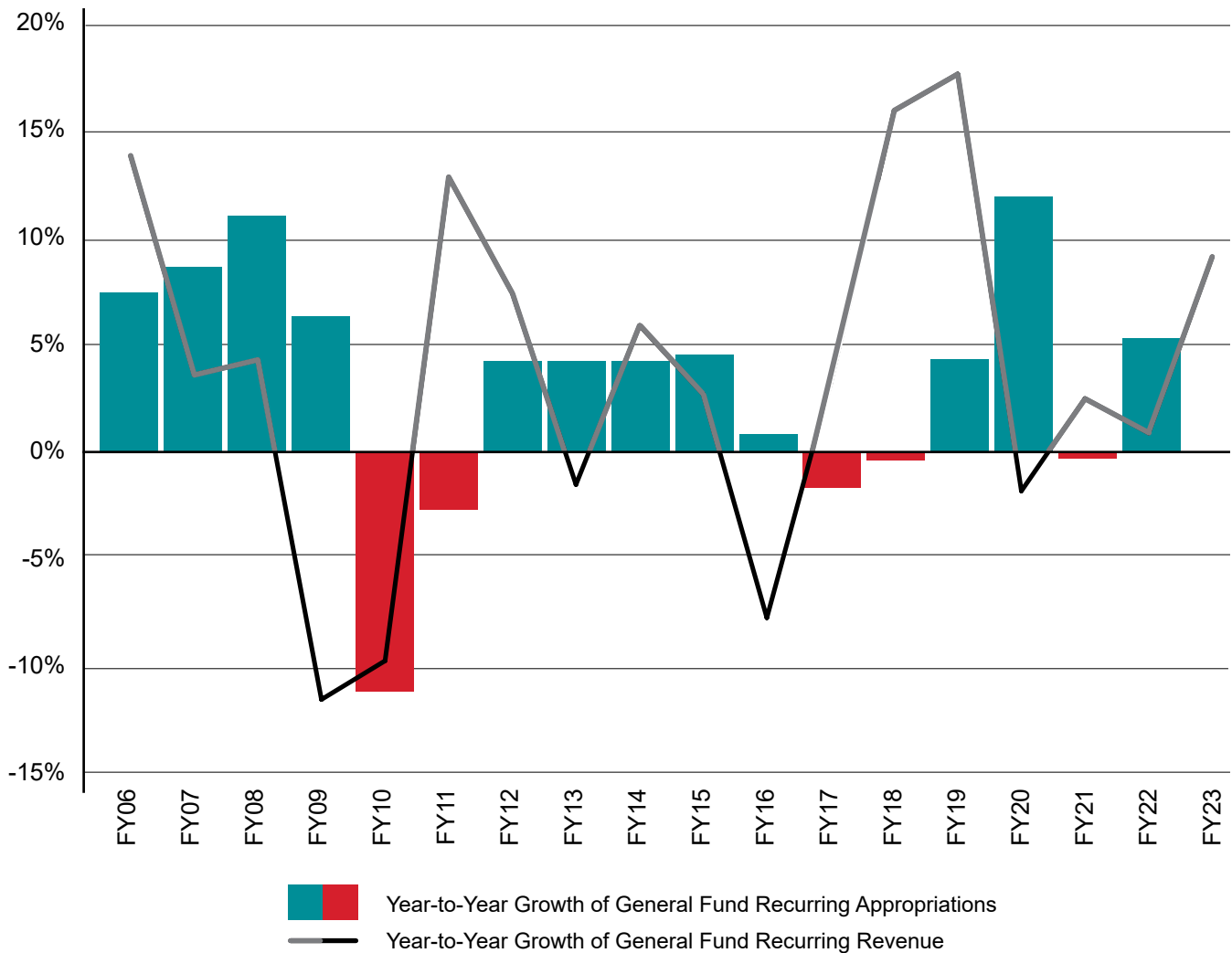
We cannot continue oscillating between revenue booms and busts. New Mexico needs more stable and fair revenues to make sure we can provide the necessary programs and services that help New Mexico's families thrive, regardless of the global price of oil.



FIGURE I

Downturns in New Mexico’s Revenues have Coincided with Big Budget Cuts

Annual Growth in General Fund Recurring Revenue and Appropriations (FY2006-FY2023)



Note: Amounts for FY21, FY22 and FY23 are estimates
 Source: Legislative Finance Committee Files
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2. A NUMBER OF INDICATORS SHOW THE OIL AND GAS INDUSTRY IS IN A LONG-TERM DECLINE

New Mexico’s over-reliance on one industry’s revenues is a threat to our fiscal health because research shows that the oil and gas industry is in a long-term decline – a decline that began even before the pandemic. The steady growth of renewables and changes in energy consumption patterns mean we

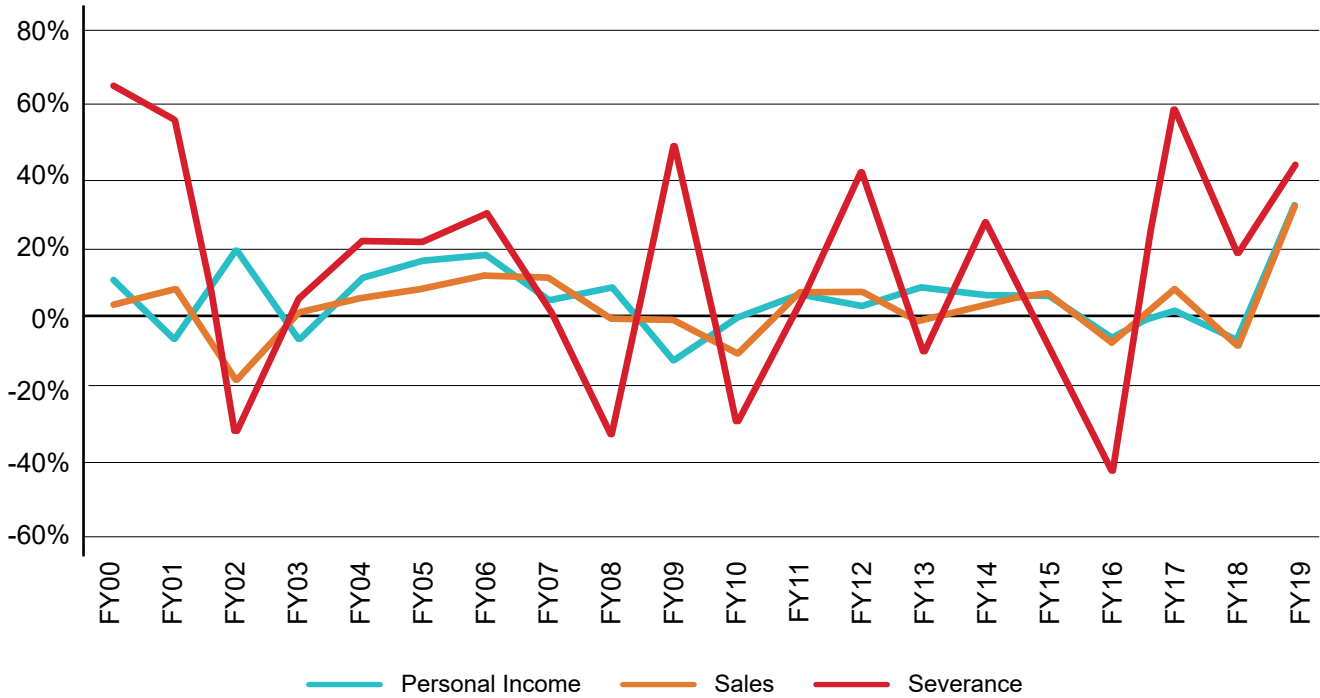
cannot continue to rely on this industry as an ongoing source of revenue.

As the energy landscape changes to one that accounts for the growing threat of climate change, “the combined effects of high infrastructure costs, over-production and substantial shifts in the energy market have permanently weakened the oil and gas industry’s revenues and profitability,” according to a recent report.³

FIGURE II

Of All Our State's Major Revenue Sources, Oil and Gas Extraction is the Least Dependable

Year-over-Year Percent Change in New Mexico's Major Tax Revenue Sources (FY2000-FY2019)



Source: *Tax Revenue Swings Complicate State Budgeting*, Pew Trusts, September 2021
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The industry has certainly contributed significantly to our revenues over the years, but our children, our classrooms, and our communities deserve more funding reliability. Lawmakers cannot wait for these revenues to dissipate, and instead need to be forward-thinking in replacing these revenues with fair and stable sources.

3. FOR THE HEALTH AND WELL-BEING OF OUR CHILDREN, NEW MEXICO NEEDS TO TRANSITION AWAY FROM FOSSIL FUELS

In 2018, the oil and gas sector was responsible for 53% of greenhouse gas emissions in New Mexico, according to New Mexico's climate report. The sector with the next-largest emissions, transportation, was only responsible for 14%.⁴

These emissions are a threat to public health and pollute our air, which can cause respiratory illness and other acute and chronic health problems, especially among children and the elderly. Oil and

gas production can also leak toxic substances into the soil and our drinking water sources, negatively impacting the health of our communities and wildlife.

Current and proposed climate change mitigation strategies will help reduce the state's overall emissions profile, but reaching the state's long-term targets will require ambitious action and increased regulations to limit the oil and gas industry's ability to pollute our air, land, and water.



4. THE STATE HAS MANY UNMET REVENUE NEEDS, AND THEY'RE ONLY EXPECTED TO GROW

Our state not only needs stable revenue to reliably invest in our future, but also to meet the outstanding financial needs we have at the moment, many of which impact the health and well-being of our children and families.

These include: massive infrastructure needs like fixing our roads, bridges, and water systems, and mitigating and adapting to climate change; bold, equitable, and long-term investments in our education system to address the needs of the *Yazzie-Martinez* lawsuit; addressing challenges with state employee vacancies, compensation, and retention rates; outstanding claims at the Taxation and Revenue Department protesting income tax amounts owed; public retirement fund needs; and film credit payments which are anticipated to grow.

In addition, the state's budget must grow by at least 3% each year to account for inflation and population growth in order for the state to offer the same level of services.⁵

5. RAISING ADEQUATE AND SUSTAINABLE REVENUE CAN HELP PROMOTE EQUITY IN OUR COMMUNITIES

The pandemic and corresponding economic downturn have illuminated the long-standing health and

economic inequities that exist for our communities of color. These inequities ultimately stem from racism's harmful legacy and the ongoing inequality of opportunity that plagues our state.

Disparities are created and furthered by government policies and practices – from slavery and the confiscation of tribal land and resources, to Jim Crow laws, red-lining policies and the segregation of Black families in lower-value neighborhoods, lending discrimination to make purchasing homes or starting businesses difficult if not impossible, and tax cuts that favor wealth over wages.

Tax policy is an important equity tool to help remedy these disparities because it decides who pays their fair share of taxes, who doesn't, and who benefits most from the way the system is structured. Fortunately, New Mexico's lawmakers can help provide more opportunities for communities of color by enacting tax and budget policies that advance equity.⁶

In order to build a more equitable New Mexico, policymakers need to prioritize our communities of color instead of the wealthy and well-connected, who are disproportionately white, when considering tax cuts, and changes to deductions, credits, and rates. By asking those with the most resources to contribute a little more, we can use this reliable revenue to budget with our values and invest in education, health care, public safety, and economic development, which all benefit our communities and classrooms, while building a stronger, more prosperous New Mexico for all.



RECOMMENDATIONS FOR RAISING FAIR, SUSTAINABLE, AND ADEQUATE REVENUE OUR STATE CAN RELY UPON

There are many common-sense ways to raise reliable revenue that can be used to educate our workforce, create jobs, and bolster our economy in a way that is sustainable, forward looking, and better supports child well-being and environmental health. Income, wealth, property, sales, and excise taxes can all be reformed in a way that asks more from those with the means to pay their fair share. For a more in-depth description of each of the options listed below, please see our *Fueling an Equitable Recovery* policy brief at nmvoices.org.

Personal Income Tax

- Raise income tax rates for the state's highest income earners
- Reform or repeal itemized deductions
- Require high-income earners to pay the top rate on all their income, instead of just the income that falls in the top bracket
- Decouple from federal "Opportunity Zone" tax breaks

Wealth Taxes

- Fully repeal the capital gains preference
- Enact an estate or inheritance tax
- Enact a "mansion tax" on high-value or second homes

Corporate Income Tax

- Increase the corporate income tax rate
- Establish a corporate minimum tax of \$500 or more
- Establish a minimum tax on large S-corps and LLCs
- Include foreign tax havens in mandatory combined reporting

Gross Receipts Tax

- Repeal wasteful and ineffective tax breaks

Excise Taxes

- Raise the gas tax
- Raise the motor vehicle excise tax so it's more in line with neighboring states
- Raise tobacco, e-cigarette, and alcohol taxes

Property Taxes

- Enact a real estate transfer tax on second or high-value homes
- Adopt different property tax rates for different kinds of property

Other Tax and Revenue Options

- Tax the full rental rate of hotels booked online
- Increase severance taxes (royalty payments) on natural resource extraction
- Enact a new tax on diesel fuel
- Enact a heavy trucks permit fee



Diversifying our economy and revenue streams cannot happen overnight nor can it happen quickly, but it must happen eventually if we want to have a stable, sustainable way to truly invest in the programs that matter most to our families now and into the future.

We cannot afford to be so reliant on oil and gas revenues. Instead, we need to evaluate our tax code and ensure that it is working for all New Mexicans and that we have enough revenue to build the best possible future for our state – one that robustly supports the programs that are most important to our children’s and our families’ well-being and support opportunities for them to thrive and reach their full potential.

Endnotes

- 1 Legislative Finance Committee analysis based on February 2021 Consensus Revenue Estimate
- 2 “Tax Revenue Swings Complicate State Budgeting,” Pew Charitable Trusts, July 27, 2021
- 3 *New Mexico’s Risky Reliance on Oil Revenue Must Change: Industry Fundamentals Point to Long-Term Decline*, Institute for Energy Economics and Financial Analysis, pg. 3, October 2020
- 4 “Closing New Mexico’s Emissions Gap,” presentation to the Water and Natural Resources Committee by Rama Zakaria, November 2020
- 5 “Post-Session Fiscal Report” presented to the Revenue Stabilization and Tax Policy Committee by the Legislative Finance Committee, June 9, 2021
- 6 *Tax Policy: A Powerful Tool to Advance Racial Equity in New Mexico*, NM Voices for Children, December 2020



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