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## FISCAL IMPACT REPORT

**BILL NUMBER:** House Bill 106

**SHORT TITLE:** Home-Based Child Care Income Tax Credit

**SPONSOR:** Duncan/Terrazas

**LAST UPDATE:** \_\_\_\_\_ **ORIGINAL DATE:** 02/03/26 **ANALYST:** Graeser/Faubion

### REVENUE\* (dollars in thousands)

Type	FY26	FY27	FY28	FY29	FY30	Recurring or Nonrecurring	Fund Affected
PIT	\$0.0	(\$665,000.0)	(\$685,000.0)	(\$705,000.0)	(\$725,000.0)	Recurring	General Fund

Parentheses indicate revenue decreases.

\*Amounts reflect most recent analysis of this legislation.

### ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT\* (dollars in thousands)

Agency/Program	FY26	FY27	FY28	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
ECECD	\$0	\$251.0	\$251.0	\$502.0	Recurring	General Fund
TRD/ACD	\$0	Up to \$150.0	Up to \$150.0	Up to \$300.0	Recurring	General Fund

Parentheses ( ) indicate expenditure decreases.

\*Amounts reflect most recent analysis of this legislation.

### Sources of Information

LFC Files

#### Agency or Agencies Providing Analysis

Early Childhood Education and Care Department

Ethics Commission

#### Agency or Agencies That Were Asked for Analysis but did not Respond

Public Education Department

Taxation and Revenue Department

## SUMMARY

### Synopsis of House Bill 106

House Bill 106 (HB106) creates a new personal income tax credit, the home-based child care income tax credit, for taxpayers who do not enroll a dependent child in a state-funded or private child care facility or a state-funded or private pre-kindergarten program. The credit is available for each month a dependent child is not eligible to enroll in public school.

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The credit is set at \$1,000 per month per eligible dependent child. An eligible child is defined as age five or younger and not eligible to enroll in public school kindergarten. The maximum annual benefit is \$12 thousand per child, and the credit is fully refundable.

Taxpayers must apply to the Early Childhood Education and Care Department (ECECD) for certification of eligibility. Certified taxpayers would then claim the credit as part of their annual personal income tax filing with the Taxation and Revenue Department.

The provisions of the bill apply to taxable years beginning on or after January 1, 2026, and the bill does not include a sunset date.

## FISCAL IMPLICATIONS

This bill creates a fully refundable home-based child care income tax credit of \$1,000 per month per eligible dependent child, or up to \$12 thousand per child annually. Because the credit is refundable, the full value of the credit represents a potential reduction to general fund revenues. The fiscal impact therefore depends primarily on the number of children who meet the bill's eligibility criteria and on household participation rates.

To bound the potential impact, LFC developed two complementary approaches to estimating the number of eligible children. The first approach begins with the estimated population of children under age five in New Mexico, approximately 111,500 based on birth cohort data. LFC then subtracts an estimated 45,000 children under five who are enrolled in Early Childhood Education and Care Department (ECECD)-registered child care homes or licensed facilities, adjusted to reflect the recent expansion of the universal child care program. The remaining approximately 66,500 children are not currently enrolled in registered or licensed care and could therefore meet the bill's requirement that the dependent child not be enrolled in a state-funded or private child care facility or pre-kindergarten program. If all children in this residual population were eligible and claimed the credit for a full year, the resulting maximum annual fiscal impact would be approximately \$798 million.

Recognizing that this residual population likely overstates true eligibility and participation, LFC also considered workforce participation as a proxy for likely utilization. U.S. Census Bureau estimates indicate that approximately 60 percent of children under age five have all available parents participating in the workforce in New Mexico, implying that 40 percent have an available parent not in the workforce. Applying this share to the estimated under-five population yields approximately 44,600 children who could be eligible for home-based care under the bill. At the annual credit amount of \$12 thousand per child, this approach yields an estimated annual fiscal impact of approximately \$535.2 million. This scenario is more closely aligned with the bill's intent to support families with an available parent providing care at home but may underestimate eligibility if some households with an available parent are nonetheless enrolled in registered or licensed care.

Given the uncertainty surrounding actual participation, certification outcomes administered by ECECD, partial-year eligibility, shifting from out-of-home care to in-home care, and compliance with the bill's requirements, LFC treats these two estimates as bookends rather than point forecasts. As a planning assumption, LFC considers the midpoint between the two scenarios—approximately \$665 million annually—to represent a reasonable central estimate of the likely fiscal exposure. Actual impacts could be higher or lower depending on take-up rates, behavioral

responses, and administrative enforcement. This estimate was grown by an inflation factor to account for the indexing of credit.

This bill creates a tax expenditure with a cost that is difficult to determine but likely significant. Estimating the cost of tax expenditures *ex ante* 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 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. LFC has serious concerns about the substantial risk to state revenues from tax expenditures and the increase in revenue volatility from erosion of the revenue base. The committee recommends the bill adhere to the LFC tax expenditure policy principles for vetting, targeting, and reporting or action be postponed until the implications can be more fully studied.

## **SIGNIFICANT ISSUES**

HB106 creates a fully refundable home-based child care income tax credit of \$1,000 per month per eligible dependent child under age five who is not enrolled in public school, a state-funded or private child care facility, or a state-funded or private pre-kindergarten program. The policy intent of the bill appears to be to reduce the financial necessity for parents of very young children to participate in the workforce by directly compensating families who provide care at home.

Some dual-earner households may elect for one parent to remain at home rather than utilize paid child care, reducing demand for publicly supported or subsidized child care slots. To the extent this occurs, the state could experience some offsetting savings on the appropriations side from reduced utilization of universal or subsidized child care programs. However, an unknown share of beneficiaries—particularly married households with toddlers—already have one parent staying home. In those cases, the credit would primarily compensate behavior that is already occurring rather than induce new labor-force or child-care decisions. In tax policy terms, this reflects “buying the base,” where a substantial portion of program cost is attributable to existing electors rather than behavioral change, increasing overall fiscal exposure without a commensurate change in outcomes.

The bill’s eligibility structure is closely tied to New Mexico’s early education framework. Children must be under the age at which public school kindergarten is an option, which generally requires a child to be five years old before September 1 of the school year, with limited early enrollment options thereafter. As a result, the bill applies to a population currently served largely by private child care providers or informal care arrangements. While the credit may shift some families away from formal care, it does not directly expand early learning capacity and could affect enrollment stability for private providers, particularly smaller or rural providers that rely on consistent participation to cover fixed costs.

Affordability concerns underpin the bill’s rationale. Federal guidance from the U.S. Department of Health and Human Services considers child care “affordable” if it costs no more than 7 percent of household income, yet many families spend substantially more. In New Mexico, annual costs for center-based care for toddlers and preschoolers can exceed \$10,000 per child. While the credit could offset these costs for eligible families, it would also provide the same benefit to households that may already have the financial means to remain single-income, raising

questions about targeting and distributional efficiency, particularly in the absence of income limits.

The size and refundability of the credit raise significant administrative, compliance, and fiscal control considerations. The credit may reach \$12 thousand per child per year and is fully refundable, meaning taxpayers may receive a net payment from the state even with no income tax liability. Refundable credits operate outside the annual appropriations process, and utilization could grow more quickly than anticipated, complicating revenue forecasting and reducing budget flexibility.

There is also a heightened risk of improper or fraudulent claims. While verification of a child's age could be accomplished through birth records, detecting under-the-table income or informal employment would be difficult, particularly if fewer W-2s are issued as parents exit the formal workforce. In addition, verifying compliance for families utilizing informal or unregistered child care arrangements would be challenging. The bill conditions eligibility on a child not being enrolled in a state-funded or private child care or pre-kindergarten program, but many families rely on care provided by relatives, neighbors, home-based nannies, or unlicensed providers that operate outside formal reporting systems and do not generate enrollment records. Distinguishing between true home-based parental care and informal third-party care would therefore be difficult to administer and enforce, increasing the risk of improper claims and placing additional verification burdens on both ECECD and the Taxation and Revenue Department (TRD).

Finally, the creation of a fully refundable tax credit raises constitutional considerations under the Anti-Donation Clause of Article IX, Section 14 of the New Mexico Constitution. Courts have held that both refundable and non-refundable tax credits may violate the clause when they function as targeted subsidies rather than bargained-for exchanges. Because a refundable credit can result in a negative tax liability—requiring direct payments from the state—the constitutional analysis turns on whether the state receives sufficient consideration in exchange for the transfer. Anticipated public benefits alone are not sufficient to remove a transfer from the Anti-Donation Clause's scope. It is unclear whether the credit's conditions would be deemed sufficiently contractual in nature or whether any enumerated exceptions would apply, and the bill could therefore be subject to constitutional scrutiny.

## **PERFORMANCE IMPLICATIONS**

The LFC tax policy of accountability is met with the bill's requirement to report annually to an interim legislative committee regarding the data compiled from the reports from taxpayers taking the credit and other information to determine whether the credit is meeting its purpose. These data will be published in the annual tax expenditure report required by 7-1-84 NMSA 1978.

## **ADMINISTRATIVE IMPLICATIONS**

HB106 requires ECECD to certify eligibility every month for each child, creating a steady stream of applications, verification tasks, and data management responsibilities resulting in a demand for new staffing, updated technology systems, and stronger coordination with TRD to ensure accurate and timely processing of refundable credits. Verifying that children are not enrolled in any public or private child care or pre-K program also adds complexity, increasing the need for agency-wide data checks and clear procedures to prevent errors or duplicate claims.

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Because the taxpayer must apply for a certification of eligibility from the ECECD for the tax credit, ECECD estimates that three (3) additional Full Time Employees (FTEs) will be required to process certifications of eligibility. ECECD estimates that the cost of each FTE will be approximately \$83,680 each, per year, including benefits, for a total of \$251,040 without which ECECD cannot absorb the additional work required.

## OTHER SUBSTANTIVE ISSUES

In assessing all tax legislation, LFC staff considers whether the proposal is aligned with committee-adopted tax policy principles. Those five principles:

- **Adequacy:** Revenue should be adequate to fund needed government services.
- **Efficiency:** Tax base should be as broad as possible and avoid excess reliance on one tax.
- **Equity:** Different taxpayers should be treated fairly.
- **Simplicity:** Collection should be simple and easily understood.
- **Accountability:** Preferences should be easy to monitor and evaluate.

In addition, staff reviews whether the bill meets principles specific to tax expenditures. Those policies and how this bill addresses those issues:

Tax Expenditure Policy Principle	Met?	Comments
<b>Vetted:</b> The proposed new or expanded tax expenditure was vetted through interim legislative committees, such as LFC and the Revenue Stabilization and Tax Policy Committee, to review fiscal, legal, and general policy parameters.	✗	No record of interim committee hearing could be found.
<b>Targeted:</b> The tax expenditure has a clearly stated purpose, long-term goals, and measurable annual targets designed to mark progress toward the goals.  Clearly stated purpose Long-term goals Measurable targets	✗ ✗ ?	Purpose is implicit – to encourage stay-at-home parents.
<b>Transparent:</b> The tax expenditure requires at least annual reporting by the recipients, the Taxation and Revenue Department, and other relevant agencies	✓	Will be published in the Tax Expenditure Report required by 7-1-84 NMSA 19878
<b>Accountable:</b> The required reporting allows for analysis by members of the public to determine progress toward annual targets and determination of effectiveness and efficiency. The tax expenditure is set to expire unless legislative action is taken to review the tax expenditure and extend the expiration date.  Public analysis Expiration date	✗ ✗	The public will be confused by the increase in the tax expenditure and a corresponding reduction in child care subsidies.
<b>Effective:</b> The tax expenditure fulfills the stated purpose. If the tax expenditure is designed to alter behavior – for example, economic development incentives intended to increase economic growth – there are indicators the recipients would not have performed the desired actions “but for” the existence of the tax expenditure.  Fulfils stated purpose Passes “but for” test	?	Will be plagued with buying the base Implicit purpose can be measured.
<b>Efficient:</b> The tax expenditure is the most cost-effective way to achieve the desired results.		

Key: ✓ Met   ✗ Not Met   ? Unclear