Tax Expenditure Assessment (Tax-E) Introduction and Summary

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Roadmap

- Tax expenditures and motivation for tax expenditure assessments
- Tax expenditure assessments – overview and summary
- Terms and definitions
- Overview of June tax expenditure assessments
  - High-wage jobs tax credit
  - Rural job tax credit

Tax Expenditures Key terms

A tax expenditure is preferential tax treatment that costs the state money.

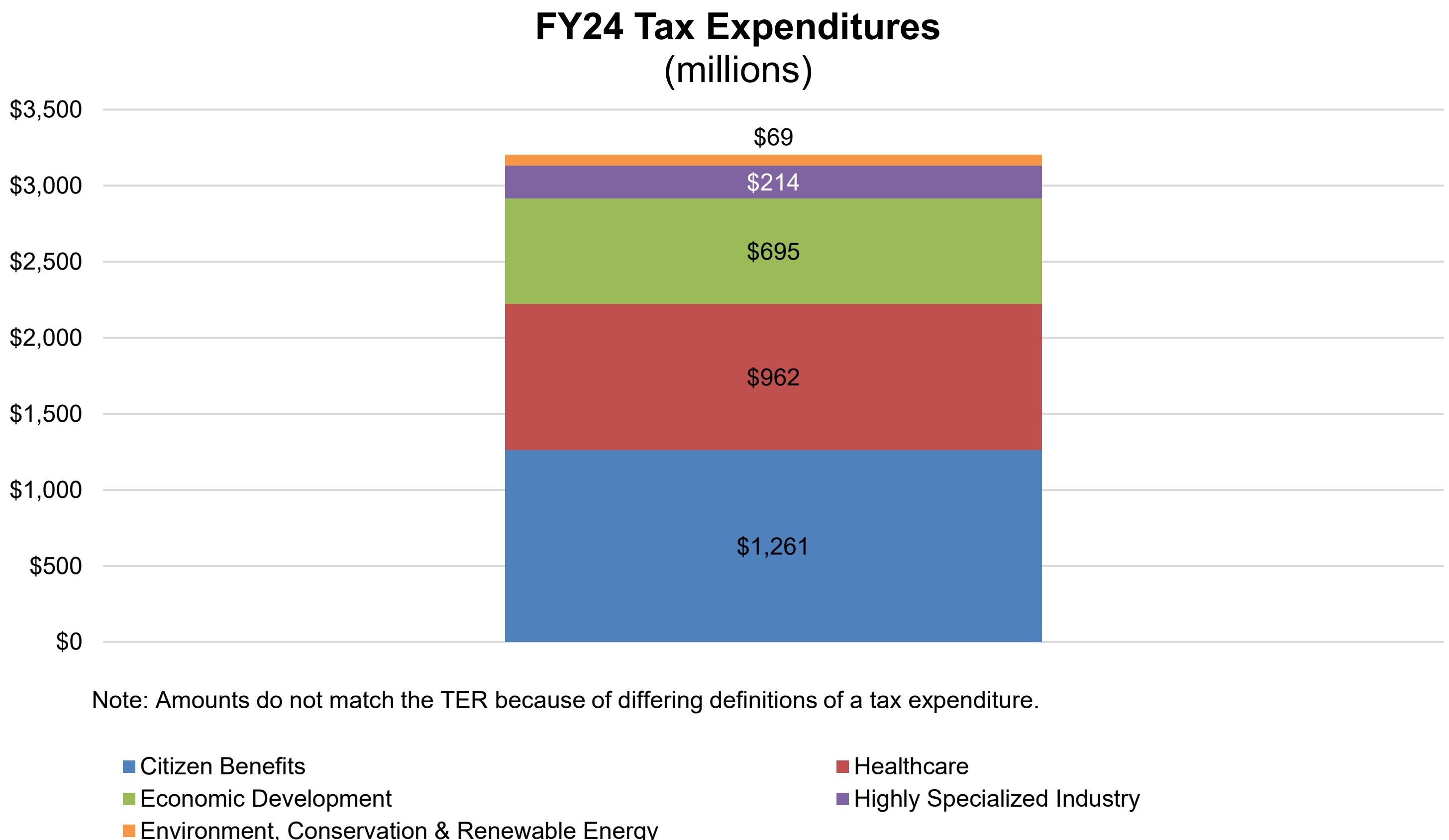
Examples include:

- *Credits:* dollar-for-dollar amounts taxpayer's claim on their tax return to reduce the tax they owe.
    - Child tax **credit**: a refundable credit for taxpayers with children equal to between $25 and $600 depending on income.

- *Exemptions:* provisions that eliminate a taxpayer's obligation to register, report, and/or pay.
    - Low- and middle-income taxpayers' **exemption** from PIT: taxpayers with incomes under either $36,667 (single) or $55,000 (married) may exempt some income that they would pay tax on.

- *Deductions:* provisions that reduce liability by eliminating certain transactions or income from amounts taxpayers are required to report
    - Dependent **deduction** from PIT for certain dependents: taxpayers may claim an up to $4,000 deduction if they meet dependent requirements.

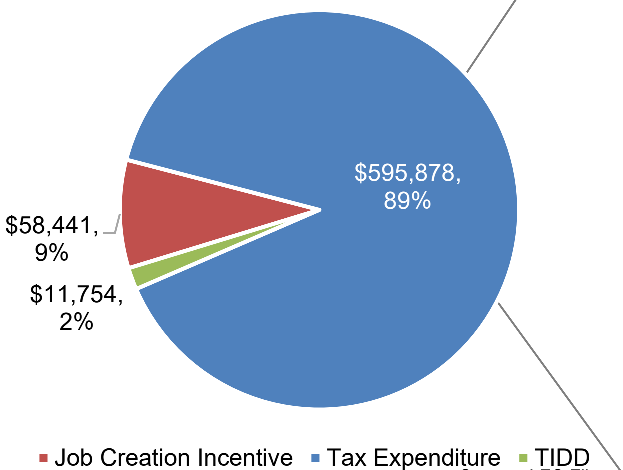
Tax expenditures make up a large share of the state budget



Source: LFC Analysis of TRD TER

Tax expenditures comprise most of economic development investments

Recurring Economic Development Investments by Type FY24
(thousands)



Source: LFC Files

FY24 State Economic Development Tax Expenditures
(in thousands)

Tax Expenditure	Expenditure	Share of Total
Sales to manufacturers GRT deduction	$200,788	33.7%
Manufacturer's CIT apportionment	$104,401	17.5%
Film tax credit	$102,166	17.1%
Sales of services to manufacturing	$84,098	14.1%
LEDA GRT distributions	$23,084	3.9%
Medical supplies GRT deduction	$19,600	3.3%
Directed energy and satellites GRT deduction	$14,039	2.4%
Technology jobs & R&D credit	$11,191	1.9%
★ High-wage jobs tax credit	$11,185	1.9%
Aircraft sales GRT deduction	$4,273	0.7%
Sale of software development services GRT deduction	$3,673	0.6%
Investment credit	$3,615	0.6%
Lab partnership with small business tax credit	$2,300	0.4%
Sales to state-chartered credit unions deduction	$2,102	0.4%
Future distribution from an estate or trust to a nonresident beneficiary deduction	$1,852	0.3%
Apportionment election of CIT for headquarters	$1,657	0.3%
Hosting worldwide websites deduction	$1,480	0.2%
Jet fuel GRT deduction	$1,347	0.2%
Angel investment PIT credit	$875	0.1%
Investment management and advisory services GRT deduction	$700	0.1%
★ Rural job tax credit	$637	0.1%
Small business Saturday GRT deduction	$542	0.1%
Border zone trade-support companies GRT deduction	$180	<0.1%
Technology readiness GRT credit	$93	<0.1%
Total	**$595,878**	

Source: LFC Files

Tax expenditure assessments have a narrow scope, with opportunity for future work

Tax Expenditure Assessments contain:

- Trends in expenditures and claims
- Analysis of fiscal and economic impact:
  - Economic return on investment (ROI)
  - Return in revenue
- Whether the credit meets tax policy best practices
  - Purpose statement
  - Design elements

Provides snapshot of what the state is getting for its investment

What Tax Expenditure Assessments do not contain:

- Recommendations
- Cost-benefit analysis
- State comparisons
- Causal analysis

Potential opportunities for future study

Economic and Fiscal Impact Terminology

Return in revenue

- Reflects how much state revenue increases over a 20-year period because of the state's investment in a tax expenditure after accounting for the costs of the expenditure
- A negative return in revenue means the increase in revenue is not greater than the cost of the expenditure.
- A -25% return in revenue means that for every $1 spent, the state forgoes 25 cents and recovers 75 cents.

Economic Return on investment (ROI)

- Reflects the increase in state GDP over a 20-year period because of the growth in the economy after accounting for the costs of the expenditure
- A 25% return on investment means that for every $1 spent, the state economy grows by 25 cents.

Economic and Fiscal Impact Terminology

Cost-Benefit Analysis (CBA)

- A policy assessment method that quantifies, in monetary terms, the value of all consequences of a policy to the public.
- Useful in comparing apples-to-apples across policy areas.
- Considers all lifetime benefits and costs, including opportunity costs, over a decades-long horizon.

<u>Tax Expenditure Assessments do not contain a CBA</u>

- As a result, Tax Expenditure Assessments do not make statements on whether an expenditure is “worth” or “not worth it,” but provide a program inventory.
- CBA is the gold standard for answering these types of questions and staff can begin to develop them for future analysis.

What do these reports specifically assess?

Example Tax-E Summary Table

FY24 Tax Expenditure	$5M
FY24 Number of Claims	100
Jobs Created	200
Economic ROI	50%
Return in Revenue	-50%
Usage Trends	
1-Year Change	+10%
3-Year Average Change	-15%
Meets Purpose	●
Design	
Has expiration date	●
Has expenditure cap	○
Targets distressed areas	◐
Targets export-based industry	●
Data Availability *Are requirements being met?*	○
Data Reliability *Is data reported separately?*	●

From TRD's Tax Expenditure Report

Calculated using REMI, an economic modeling software

Trend in claims over given period of time

Is there a purpose statement? Is the purpose being met? Considers usage, jobs created, etc.

Based on LFC tax policy & tax expenditure policy principles and best practices criteria for assessing tax expenditures

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QUESTIONS?

Appendix: LFC Tax Policy Principles

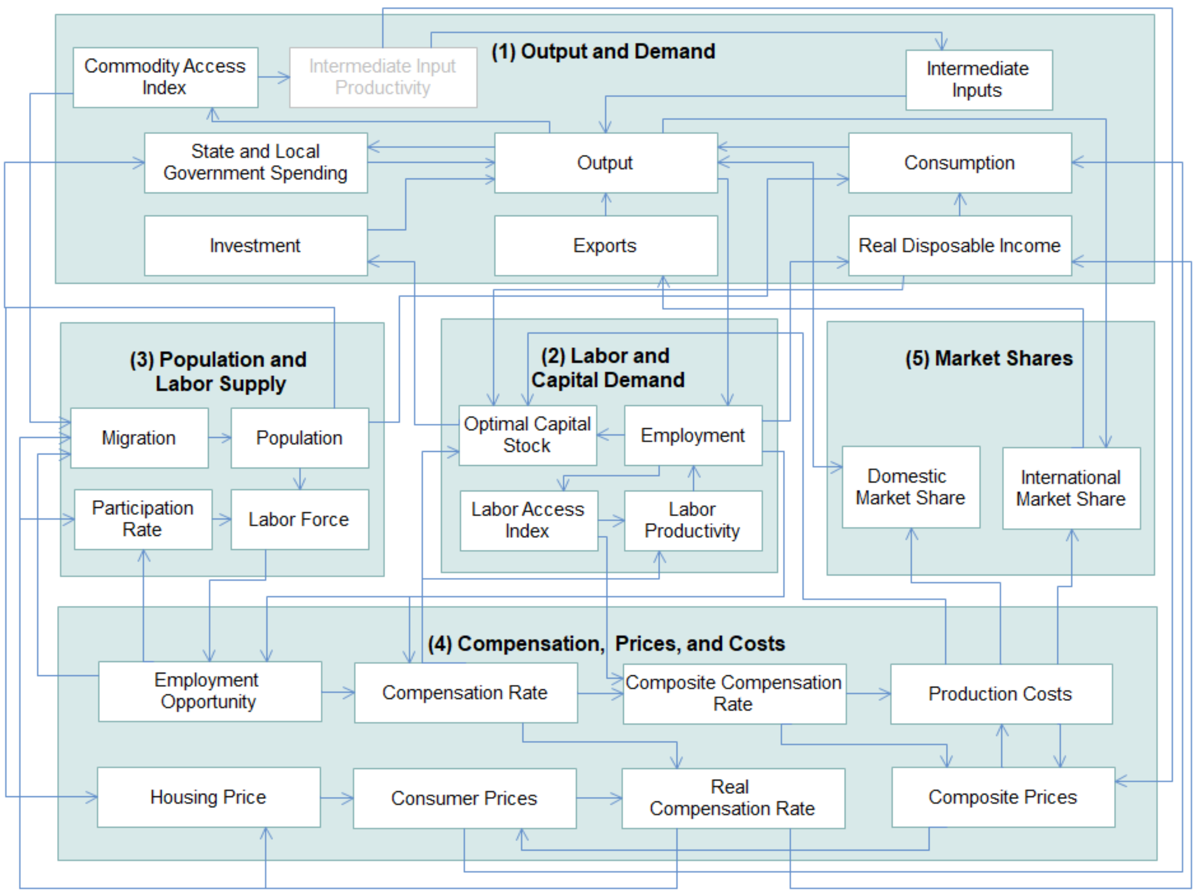
- **Adequacy**: Revenue should be adequate to fund needed government services.
- **Efficiency**: Tax base should be as broad as possible and avoid excess reliance on one tax.
- **Equity**: Different taxpayers should be treated fairly.
- **Simplicity**: Collection should be simple and easily understood.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

Appendix: LFC Tax Expenditure Policy Principles

- **Vetted**: The proposed new or expanded tax expenditure was vetted through interim legislative committees.
- **Targeted**: The tax expenditure has a clearly stated purpose, long-term goals, and measurable annual targets designed to mark progress toward the goals.
- **Transparent**: The tax expenditure requires at least annual reporting by the recipients, the Taxation and Revenue Department, and other relevant agencies.
- **Accountable**: 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.
- **Effective**: 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.
- **Efficient**: The tax expenditure is the most cost-effective way to achieve the desired results.

Appendix: REMI Model Overview

REMI Model Linkages



Tax·E Tax Expenditure Assessment
Analysis of key state tax credits, exemptions, and deductions by the Legislative Finance Committee

Rural Job Tax Credit

Background

Brief Description. The rural job tax credit provides an incentive to businesses opening or expanding in rural areas equal to either 12.5 percent or 25 percent of up to $16 thousand in wages per qualifying job, depending on where the job is performed or based.

Created: 2007 and amended in 2013, and 2021

Expires: No expiration date.

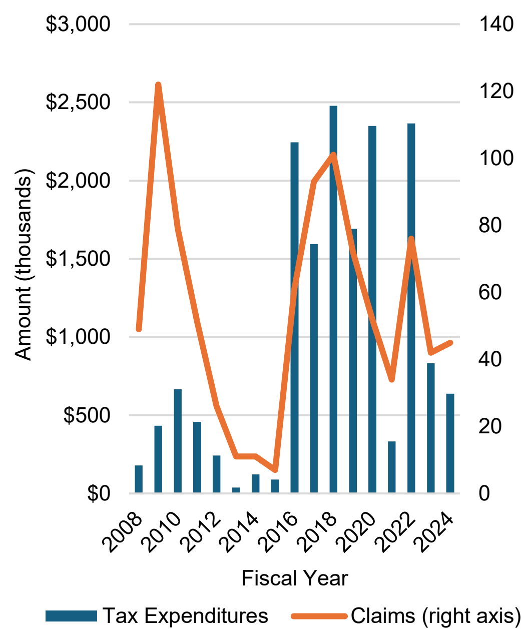
Impact Analysis Summary

In FY24, businesses received $637 thousand in state support through the credit. Over the last ten years, businesses received an average of $1.2 million in state support through the credit each year. The credit is estimated to increase statewide employment by 20 jobs per year on average because of lower business costs that encourage job creation. The average cost per job is $30 thousand. The credit is estimated to increase state personal income by $1.1 million, on average, because of higher wage earnings, increased business profits, and increased property income. The estimated net annual impact in state GDP attributable to the program is $1.9 million. The economic return on investment (ROI) is estimated to be 35 percent, meaning for every $1 spent on the credit, the New Mexico economy grows by 35 cents. The estimated annual return in revenue is -83 percent, meaning that for every $1 spent, the state forgoes 83 cents and recaptures 17 cents of state tax revenue.

Economic Impact Analysis Summary

FY24 Expenditure	***FY24 Claims***
$0.6 M	*45*
Economic ROI	***Return in Revenue***
35%	*-83%*
For every $1 spent, the state economy grows by 35 cents.	For every $1 spent, the state foregoes 83 cents and recaptures 17 cents in state tax revenue.

Tax Expenditures and Claims of Rural Job Tax Credit



THIS REPORT summarizes key fiscal and economic impact information of state tax expenditures. These brief summaries are prepared on an ongoing basis for policymakers to identify—and request further study of—larger policy issues. The primary sources of information are the New Mexico Tax Expenditure Reports from 2012-2024, accessible on the Taxation and Revenue Department's website, and other state and national economic data. Detailed methodology of this report can be found at the LFC Revenue, Economic Reports, and Tax Policy website.

This Issue: **Rural Job Tax Credit**

Credit Overview and Legislative History. The rural job tax credit was first enacted in 2007 to encourage business expansion in rural areas of the state. It provides a refundable tax credit to businesses eligible for the Job Training Incentive Program equal to either 12.5 percent or 25 percent of up to $16,000 in wages per qualifying job, depending on the area's population. Employers in Tier 1 areas (population under 15 thousand) receive the full 25 percent, while those in Tier 2 areas (population between 15 thousand and 30 thousand) receive 12.5 percent. The credit is disbursed incrementally, as 6.25 percent of the wages per year for up to four years for jobs in Tier 1 areas and two years for jobs in Tier 2 areas.

The credit has been amended three times. The original statute was enacted in 2000 but sunset in 2006. In 2007, the sunset provision was removed. In 2013, the credit was amended to restrict the definition of qualifying jobs to exclude jobs created due to business mergers or acquisitions. The Legislature also added a purpose statement to the credit. In 2021, the credit was amended to add certification requirements for employers, add application time limits, define "new job," and revise the definition of "qualifying job." Additionally, the 2021 amendment expanded the scope from starting new businesses to incorporate "expand[ing] existing businesses" into the purpose.

Usage Trends. From FY22 to FY24, an average of 54 claims were made per year for an average annual tax expenditure of $1.2 million. Expenditures and claims are both down from historical levels. While FY21 had fewer claims and less expenditures, between FY18 and FY20 the state spent $2.2 million on average with an average of 75 claims per year. Since 2000, the effective value of the credit has decreased by 45 percent because of inflation.

Design Analysis. The credit does not have an expenditure cap or an expiration date. While targeting rural jobs may help distressed areas, the credit could be more effective by differentiating based on need, demographics, or economic activity. The credit targets export-based industries, and agencies are meeting statutory reporting requirements.

Meets Purpose. The credit partially satisfies its purpose to encourage businesses to start new or expand existing businesses in rural areas of the state. While it has historically offered a significant benefit to rural areas, claims and expenditures have declined sharply recently, indicating the credit may not be continuing to achieve its purpose.

Summary

FY24 Tax Expenditure	$0.6M
FY24 Number of Claims	45
Jobs Created	20
Economic ROI	35%
Return in Revenue	-83%
Usage Trends	
1-Year Change	-23%
3-Year Average Change	-41%
Meets Purpose	◑
Design Elements	
Has expiration date	○
Has expenditure cap	○
Targets distressed areas	◑
Targets export-based industry	●
Data Availability *Are requirements being met?*	●
Data Reliability *Is data reported separately?*	●

Key
● Yes
◑ Partial
○ No

Note: Criteria based on LFC tax policy principles or other design, purpose, or statutory measures. Data are from New Mexico Tax Expenditure Reports from 2012-2024, accessible on the Taxation and Revenue Department's website, and other state and national economic data. Estimates on annual increase in baseline statewide employment, state GDP, and state revenues were calculated using a New Mexico-specific economic impact model using state and national employment, expenditure, and revenue information. Additional methodology details can be found at the LFC Revenue, Economic Reports, and Tax Policy website.

Future research opportunities for this tax credit include:

- Comparing the economic impacts to other tax expenditures and forms of spending
- Understanding how this credit impacts different regions of New Mexico
- Understanding the changes in claims and expenditures over time.

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High-Wage Jobs Tax Credit

Background

Brief Description. The high-wage jobs tax credit is an incentive for businesses to create and fill new high-wage jobs in New Mexico by providing a refundable tax credit equal to 8.5 percent of the wages of a new job up to $12,750.

Created: 2004 and amended in 2007, 2008, 2013, 2016, 2019, 2021, and 2025.

Expires: July 1, 2026

Impact Analysis Summary

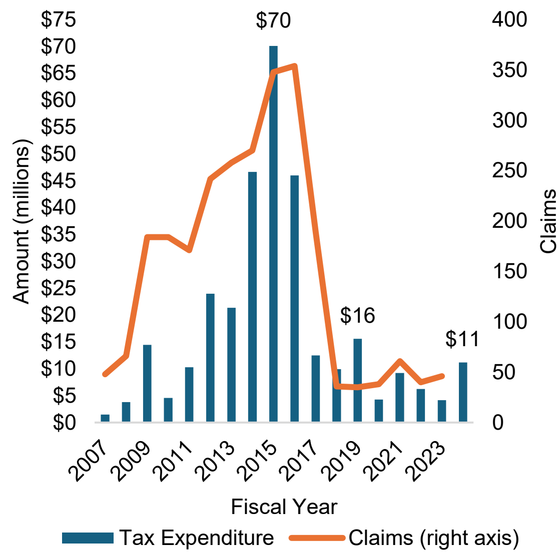
In FY24, businesses received a total of $11.2 million in state support through the credit. Over the last ten years, businesses received an average of $9.1 million in state support through the credit each year. The credit is estimated to increase statewide employment by 135 jobs per year on average because of lower business costs that encourage job creation. The average cost per job is $83 thousand. The credit is estimated to increase state personal income by $18.5 million because of higher wage earnings, increased business profits, and increased property income. The estimated annual impact in state GDP attributable to the program is $14.6 million. The economic return on investment (ROI) is estimated to be 47 percent, meaning for every $1 spent on the credit, the New Mexico economy grows by 47 cents. The estimated annual return in revenue is -83 percent, meaning that for every $1 spent, the state forgoes 83 cents and recaptures 17 cents in state tax revenue.

Economic Impact Analysis Summary

FY24 Expenditure	***FY24 Claims***
$11.2 M	*89*

Economic ROI	***Return in Revenue***
47%	*-83%*
For every $1 spent, the state economy grows by 47 cents.	For every $1 spent, the state foregoes 83 cents and recaptures 17 cents in state tax revenue.

Tax Expenditures and Claims of High-Wage Jobs Tax Credit



Source: TRD

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This Issue: **High-Wage Jobs Tax Credit**

Credit Overview and Legislative History. The high-wage jobs tax credit, provides a refundable tax credit to businesses eligible for the Job Training Incentive Program equal to 8.5 percent of wages up to $12,750 for a newly enacted high-wage job, defined as a job with wages of over $60 thousand in urban communities (population over 60 thousand people), and $40 thousand in rural communities, that are filled for 44 consecutive weeks. An employer may apply for the tax credit against tax liability from income or sales taxes.

The credit has been amended or extended six times since it was first enacted in 2004. Lawmakers made a technical change in 2007 and extended the credit in 2008. In 2013, lawmakers increased claim amounts by changing the wage qualification from $28 thousand to $40 thousand for rural employers and $40 thousand to $60 thousand for urban employees and increased the population threshold distinguishing rural from urban. Notably, the number of claims continued to rise steadily after this amendment. In 2016, lawmakers required annual filing and removed employee benefits from the calculation of wages. After these changes, claims and reimbursements went down. The most recent, significant statutory changes included lowering the reimbursement rate from 10 percent to 8.5 percent, increasing the maximum eligible benefit from $12,000 to $12,750 thousand, and reducing the job threshold from 48 to 44 consecutive weeks. Lawmakers made a minor adjustment to the definition of "threshold job" in the 2025 legislative session.

Usage Trends. From FY22 to FY24, an average of 58 claims were made per year for an average total tax expenditure of $7.2 million annually. Expenditures and claims have been relatively steady at these levels since FY18; before this, both claims and expenditures were much higher, with a peak at 348 claims and $70 million in FY15.

Design Analysis. The credit has a sunset date of July 1, 2026, but it does not have an expenditure cap. While targeting rural areas may help distressed areas, the credit could be more effective by differentiating based on need, demographics, or economic activity. The credit targets export-based industries.

Meets Purpose. The credit likely meets its purpose of "providing an incentive" for businesses to create and fill new high-wage jobs because usage and job creation has remained steady.

Summary

FY24 Tax Expenditure	$11.2M
FY24 Number of Claims	89
Jobs Created	135
Economic ROI	47%
Return in Revenue	-83%
Usage Trends	
1-Year Change	+170%
3-Year Average Change	-26%
Meets Purpose	●
Design	
Has expiration date	●
Has expenditure cap	○
Targets distressed areas	◑
Targets export-based industry	●
Data Availability *Are requirements being met?*	●
Data Reliability *Is data reported separately?*	●

Key
● Yes
◑ Partial
○ No

Note: The above findings are based on New Mexico Tax Expenditure Reports from 2012-2024, accessible on the Taxation and Revenue Department's website, and other state and national economic data. Estimates on annual increase in baseline statewide employment, state GDP, and state revenues were calculated using a New Mexico-specific economic impact model using state and national employment, expenditure, and revenue information. Additional methodology details can be found at the LFC Revenue, Economic Reports, and Tax Policy website.

Future research opportunities for this tax credit include:
- Comparing the economic impacts to other tax expenditures and forms of spending
- Comparing this credit to similar credits in other states
- Understanding how this credit impacts different regions of New Mexico