



NEW MEXICO
LEGISLATIVE
FINANCE
COMMITTEE

New Mexico's Tax Expenditure Policy Principles

Webinar: Approaches to Considering Proposed
Tax Incentives, September 10, 2019

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SETTING THE STAGE



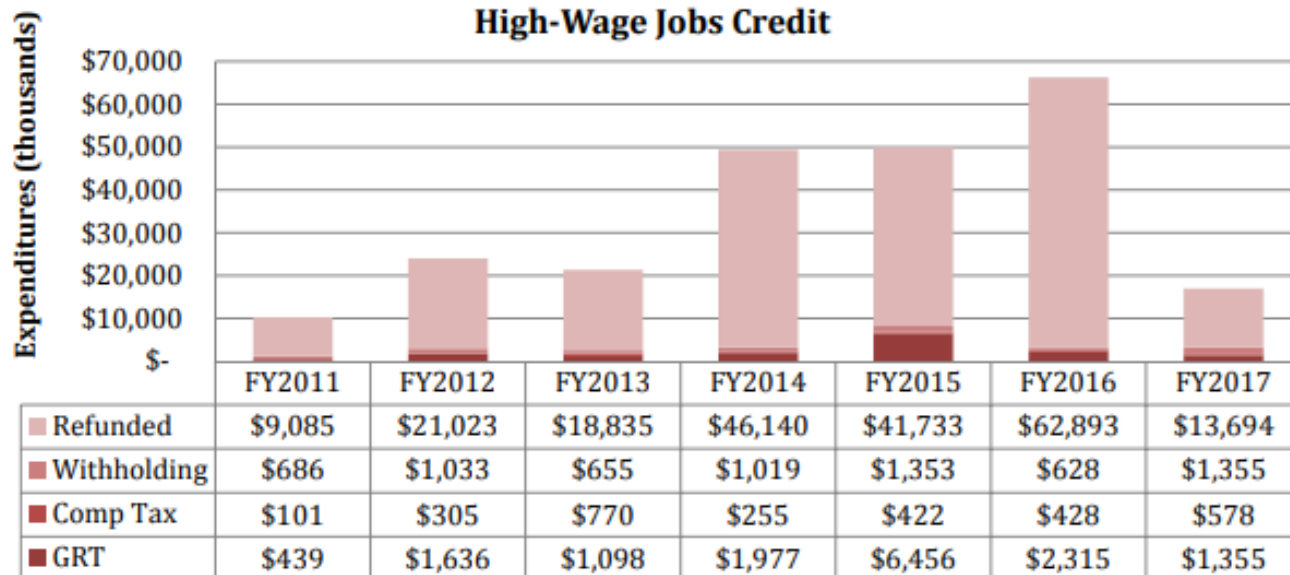
Existing tax policy principles previously used to evaluate existing and proposed policies

- 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.



Runaway costs of tax expenditures showed the need for additional policy principles

- Example: High-Wage Jobs Tax Credit
 - An economic development incentive for eligible employers who create high-wage, economic-base jobs in New Mexico
 - Cost increased from \$10 million FY11 to \$63 million by FY16
 - Significantly narrowed the eligibility requirements in a special session in 2016



Targeting the Evaluation of Tax Expenditures

CREATING NEW PRINCIPLES



Tax Expenditure Policy Principles

1. Vetted

- ✓ Through interim legislative committees
- ✓ Review fiscal, legal, and general policy parameters

2. Targeted

- ✓ Clearly stated purpose
- ✓ Long-term goals
- ✓ Measurable annual targets

3. Transparent

- ✓ Requires at least annual reporting by recipients, the tax department, and other relevant agencies



Tax Expenditure Policy Principles

4. Accountable

- ✓ Required reporting sufficient for public analysis (help determine effectiveness and efficiency)
- ✓ Expiration date (to allow for review)

5. Effective

- ✓ Fulfills the stated purpose
- ✓ If designed to alter behavior, desired actions would not have occurred “but for” the tax expenditure

6. Efficient

- ✓ Most cost-effective way to achieve desired results



The tax expenditure policy principles were endorsed by the Legislative Finance Committee in October 2018

- Principles were created by LFC staff and used in evaluation of tax expenditure bills in 2018 and 2019 legislative sessions
- Officially adopted by LFC in October 2018 with minimal debate
- LFC adopted language for all fiscal impact reports in which tax expenditure costs could not be estimated, but were likely significant

*“This bill creates or expands a tax expenditure with a cost that is difficult to determine but likely significant. LFC has serious concerns about the significant 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 be held for future consideration.**”*



- Principles also presented to the interim Revenue Stabilization and Tax Policy Committee, without adoption

Created an easy visual for legislators to see if a proposal meets the policy principles

LFC Tax Expenditure Policy Principle	<u>Met?</u>	Comments
Vetted	✓	
Targeted		
Clearly stated purpose	✓	
Long-term goals	✓	
Measurable targets	✗	
Transparent	✓	
Accountable		
Public analysis	✗	
Expiration date	✓	
Effective		
Fulfills stated purpose	✓	
Passes “but for” test	?	
Efficient	✗	
Key: ✓ Met ✗ Not Met ? Unclear		

USING THE TAX EXPENDITURE POLICY PRINCIPLES IN PRACTICE



House Bill 165 – Modifying High Wage Jobs Tax Credit (2019 Legislative Session)

- Introduced because changes made in 2016 special session were claimed to be “too restrictive”
- Expanded eligibility and extended the sunset date
 - Still more restrictive than when costs escalated
- Estimated annual cost of ~\$10 million
- Discussed at interim committee hearings and bill provisions reviewed with legislative staff; contained an expiration date
- No stated purpose (though purpose seems evident) or reporting requirements

➤ Passed House and Senate unanimously



LFC Tax Expenditure Policy Principle	Met?
Vetted	✓
Targeted	
Clearly stated purpose	?
Long-term goals	✗
Measurable targets	✗
Transparent	✗
Accountable	
Public analysis	✗
Expiration date	✓
Effective	
Fulfills stated purpose	?
Passes “but for” test	?
Efficient	?
Key: ✓ Met ✗ Not Met ? Unclear	

Senate Bill 231 – Foster Youth Employment Tax Credit (2018 Legislative Session)

- Allows employers to claim \$1,000 credit against corporate or personal income tax for employment of qualified foster youth
- Intended to incentivize employment of foster youth
- Low estimated annual cost (\$170K annually)
- Contained a stated purpose and (some) reporting requirements
- Not vetted, no expiration date, fiscal impact report stated significant concerns on effectiveness and efficiency

➤ Passed Senate unanimously, passed House with two opposed



LFC Tax Expenditure Policy Principle	Met?
Vetted	✘
Targeted	
Clearly stated purpose	✓
Long-term goals	✘
Measurable targets	✘
Transparent	✓
Accountable	
Public analysis	?
Expiration date	✘
Effective	
Fulfills stated purpose	?
Passes “but for” test	?
Efficient	?
Key: ✓ Met ✘ Not Met ? Unclear	

House Bill 41 – Rural Health Practitioner Tax Credit Changes (2019 Legislative Session)

- Bill to expand the types of healthcare practitioners eligible for the tax credit
- Estimated annual cost ~\$8 million to \$11 million
- No stated purpose in the bill, but fairly evident
- Unclear if vetted, no required reporting
 - Initial bill had no expiration date, later amended to add a 10-year sunset
- Unclear if credit provides an incentive to stay in rural areas; size of credit makes it an unlikely incentive to move to rural areas

➤ Passed House unanimously, died in Senate



LFC Tax Expenditure Policy Principle	Met?
Vetted	?
Targeted	
Clearly stated purpose	?
Long-term goals	✘
Measurable targets	✘
Transparent	✘
Accountable	
Public analysis	✘
Expiration date	✘
Effective	
Fulfills stated purpose	?
Passes “but for” test	?
Efficient	?
Key: ✓ Met ✘ Not Met ? Unclear	

A mixed bag of results...

- ~ Some opposition to adding purpose statements to legislation
 - If added, none included long-term goals or measureable targets
- ~ Generic reporting language (annual cost and number of claimants) may not be sufficient to determine effectiveness, efficiency, or progress toward targets
- ~ General difficulty determining effectiveness and efficiency for most tax expenditures
 - Limited data availability (e.g. job creation, capital investment, economic impact, etc.), confidentiality rules
 - Difficulty determining whether incentives influenced behavior



...with signs of success

- ✓ 2019 session demonstrated more awareness and discussion of policy principles when debating tax expenditure proposals
- ✓ Increased focus on adding reporting requirements and expiration dates
 - Added to most proposals for new tax incentives in the 2019 legislative session (either initially or by amendment)
- ✓ Increased interest by the executive branch in having tax incentive proposals vetted by Legislative committees in advance



Next Steps

- Continue to inform legislators of the policy principles and how to find them in a proposal's fiscal impact analysis
- New tax expenditure reporting bill introduced in the 2019 legislative session, would have:
 - Required the tax department to continue its publication of the annual Tax Expenditure Report
 - Allowed staff economists access to certain confidential data held by the tax, economic development, and workforce solutions departments
 - Provided funding for an additional staff economist at LFC and software for dynamic modeling of tax incentives

