# FISCAL IMPACT REPORT

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|---|---|---|---|
| | | **LAST UPDATED** | |
| **SPONSOR** | Tallman/Herndon | **ORIGINAL DATE** | 2/6/23 |
| **SHORT TITLE** | Child Income Tax Credit Increase | **BILL NUMBER** | Senate Bill 52 |
| | | **ANALYST** | Faubion |

**REVENUE***
**(dollars in thousands)**

| Estimated Revenue | | | | | Recurring or Nonrecurring | Fund Affected |
|---|---|---|---|---|---|---|
| FY23 | FY24 | FY25 | FY26 | FY27 | | |
| -- | ($11,000.0) | ($11,000.0) | ($11,000.0) | ($11,000.0) | Recurring | General Fund |

Parenthesis ( ) indicate revenue decreases
*Amounts reflect most recent version of this legislation.

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

| | FY23 | FY24 | FY25 | 3 Year Total Cost | Recurring or Nonrecurring | Fund Affected |
|---|---|---|---|---|---|---|
| | | $5.6 | | $5.6 | Nonrecurring | TRD/ITD |
| **Total** | | | | | | |

Parentheses ( ) indicate expenditure decreases.
*Amounts reflect most recent version of this legislation.

Conflicts with HB 144.

### Sources of Information
LFC Files

Responses Received From
Children, Youth, and Families Department
Taxation and Revenue Department

## SUMMARY

### Synopsis of Senate Bill 52.

Senate Bill 52 (SB52) increases the credit amount of the child income tax credit for all eligible income levels.

| Adjusted gross income is: | Current credit amount per child: | SB52 credit amount per child: |
|---|---|---|
| $0 - $25,000 | $175 | $202 |
| $25,000 - $50,000 | $150 | $173 |

| | | |
|---|---|---|
| $50,000 - $75,000 | $125 | $144 |
| $75,000 - $100,000 | $100 | $115 |
| $100,000 - $200,000 | $75 | $87 |
| $200,000 - $350,000 | $50 | $58 |
| $350,000 + | $25 | $29 |

This bill does not contain an effective date, and as a result, would go into effect June 16, 2023, (90 days after the Legislature adjourns) if signed.

## FISCAL IMPLICATIONS

The child tax credit is a graduated credit, decreasing in amount as incomes increase. Credit amounts currently range from $175 per child for the lowest income bracket to $25 per child for the highest income bracket. Senate Bill 52 increases the child income tax credit amount by approximately 15.5 percent for each income level, resulting in a range of $29 to $202 per child.

The Taxation and Revenue Department (TRD) estimated the impact of the new proposed child tax credit amounts for all taxpayers using tax return data for New Mexico taxpayers for tax years 2020 and 2021. Due to unavailability of the number of qualifying children each taxpayer has, TRD estimated the impact based on the number of exemptions each taxpayer claimed and their filing status. TRD's estimate is based on the average impact of the credit for the last two tax years. The number of children under the age of 18 has seen a 5 percent decline in New Mexico during the period 2010 to 2019, based on the U.S. Census 5-year American Community Survey. While this has been the trend, it is unknown what may be the growth or decline during the forecast period, and thus TRD assumes the impact remains flat.

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 action be postponed until the implications can be more fully studied.

Estimating the cost of tax expenditures 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 expenditure's 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.

## SIGNIFICANT ISSUES

The structure of the child tax credit creates "cliff effects" between each credit amount where taxpayers' credit amount is decreased dramatically as soon as they enter into a new income bracket. For example, someone making $24,999 will qualify for a $202 per child credit while someone making $25,001, effectively the same income, will only qualify for a $173 credit and have a higher tax liability than the other taxpayer. This creates issues with horizontal equity at those thresholds.

TRD notes the increase to the child tax credit will continue to erode horizontal equity in the state income taxes. By basing the credit on number of qualifying children, taxpayers with the same level of income are no longer treated equally. Thus, two New Mexico residents who earn the same salary may have different tax liability given how many children they choose to have in their household. The credit will provide greater tax benefit to families with greater number of children. However, child tax credit is a tool to provide economic aid to families with children and is particularly helpful to lower income families. The increase to the credit amount is more pronounced for those with lower adjusted gross income. This can be expected to result in a reduction in child poverty and hunger in the state.

## 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.

## ADMINISTRATIVE IMPLICATIONS

TRD will need to make information system changes and update forms and publications. These changes will be incorporated into annual tax year implementation and represent $5,554 in workload costs for the TRD's Information Technology Division (ITD).

## CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

SB52 conflicts with House Bill 144, which increases certain child tax credit amounts and annually adjusts the credit amounts to account for inflation.

**Does the bill meet the Legislative Finance Committee tax policy principles?**

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

**Does the bill meet the Legislative Finance Committee tax expenditure policy principles?**

1. **Vetted**: 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.
2. **Targeted**: The tax expenditure has a clearly stated purpose, long-term goals, and measurable annual targets designed to mark progress toward the goals.
3. **Transparent**: The tax expenditure requires at least annual reporting by the recipients, the Taxation and Revenue Department, and other relevant agencies.
4. **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

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| the tax expenditure and extend the expiration date.<br>**5. 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.<br>**6. Efficient:** The tax expenditure is the most cost-effective way to achieve the desired results. |

| **LFC Tax Expenditure Policy Principle** | **Met?** | **Comments** |
|---|---|---|
| **Vetted** | ? | While the current child tax credit was debated during the 2022 legislative session, this proposal has not been vetted in an interim committee. |
| **Targeted** | | |
| Clearly stated purpose | ✘ | No stated purpose. |
| Long-term goals | ✘ | No stated long-term goals. |
| Measurable targets | ✘ | No measurable targets. |
| **Transparent** | ✓ | This bill does require annual reporting to interim legislative committees. |
| **Accountable** | | |
| Public analysis | ? | As there are no stated annual targets or goals, there is nothing from which to determine progress, effectiveness, or efficiency. |
| Expiration date | ✓ | The tax exemptions expire at the end of tax year 2031. |
| **Effective** | | |
| Fulfills stated purpose | ? | As there are no stated annual targets or goals, there is nothing from which to determine effectiveness or passing of the "but for" test. |
| Passes "but for" test | ? | |
| **Efficient** | ? | No stated desired results. |
| Key: ✓ Met ✘ Not Met ? Unclear | | |

JF/rl/ne