BILL ANALYSIS AND FISCAL IMPACT REPORT
Taxation and Revenue Department

February 7, 2024

Bill: HB-294 **Sponsor:** Representative T. Ryan Lane

Short Title: Education Enrichment Tax Credit

Description: This bill creates an income tax credit for a taxpayer who purchases "educational enrichment services" for a qualified student for whom the taxpayer is a parent or guardian. Educational enrichment services are defined as recreational, social and after-school programs, including tutoring and academic and arts-related day or summer camps, that are held in New Mexico and offered by school districts or other organizations. The amount of the credit is equal to the amount paid for the services in a calendar year, not to exceed $2,000. To receive the credit, the taxpayer must obtain certification of the education enrichment services by applying to the Public Education Department (PED). The aggregate amount of credits that may be certified in a calendar year is $10 million. Applications received after this limitation has been met in a calendar year shall not be approved. The department shall compile an annual report on the credit and present it to the Revenue Stabilization and Tax Policy Committee and the Legislative Finance Committee with an analysis of the cost of the tax credit.

Effective Date: Not specified; 90 days following adjournment (May 15, 2024). Applies to tax years beginning on or after January 1, 2024.

Taxation and Revenue Department Analyst: Sara Grubbs

Estimated Revenue Impact*					R or NR**	Fund(s) Affected
FY2024	FY2025	FY2026	FY2027	FY2028		
--	($10,000)	($10,000)	($10,000)	($10,000)	R	General Fund

* In thousands of dollars. Parentheses ( ) indicate a revenue loss. ** Recurring (R) or Non-Recurring (NR).

Methodology for Estimated Revenue Impact: Qualified students, as defined in Subsection (I)(3)(a-c), on page 4, are school-age children pursuant to the Public School Code that are within the age range of 5 to 21, with eligibility dependent on birthdate, and who have not earned a high school diploma or equivalent. This credit applies to households earning less than 400% of an amount equal to 185% of the federal poverty threshold. Taxpayers with foster children or those classified as developmentally disabled qualify with no income requirements.

To estimate the number of qualified students, the Taxation and Revenue Department (Tax & Rev) assumes a school-age child is from ages 5 through 21. Tax & Rev used the Census Bureau's 2020 Decennial Census and the American Community Survey to estimate the number of persons in New Mexico ages 5 to 17, 18 to 21 and the number of disabled persons ages 18 to 21[1]. Tax & Rev assumes that developmentally disabled and foster children under the age of 18 are included in the estimate of persons ages 5 to 17 and that the number of foster children ages 18 to 21 are negligible. Tax & Rev assumes 72% of persons ages 18 to 21 graduate and reduced the number of qualified students in this age range by this percentage[2].

Tax & Rev calculated the average family size of 4.2 by dividing the total population of New Mexico by

[1] American Community Survey, ACS 5-Year Estimates, table DP05, 2022;
[2] Graduation Data – New Mexico Public Education Department (state.nm.us)

the number of New Mexico families in 2022. Assuming one family will file one tax return, Tax & Rev divided the number of qualified students by average family size to estimate the number of taxpayers.

To qualify for the education enrichment income tax credit, most taxpayers must meet income requirements based on the number of persons in the family or household. Since the average New Mexico family size is between 4 and 5, Tax & Rev assumes the average eligible maximum income is $250,800 (see table 1). 95% of New Mexico taxpayers have an income less than this resulting in approximately 97,000 taxpayers that qualify for this credit.

Table 1[3]			
Persons in family or household	**January 2024 poverty guidelines**	**185% of Poverty Guidelines to be Eligible for a Reduced Lunch**	**400% of Eligible Income**
1	$15,060	$27,861	$111,444
2	$20,440	$37,814	$151,256
3	$25,820	$47,767	$191,068
4	$31,200	$57,720	$230,880
5	$36,580	$67,673	$270,692
6	$41,960	$77,626	$310,504
7	$47,340	$87,579	$350,316
8	$52,720	$97,532	$390,128

The average annual cost of out-of-school activities to a family is dependent on income level. Tax & Rev assumes the average cost of education enrichment services is $972 per year for a family of 4 and all services qualify[4]. 97,000 taxpayers applying the average cost against personal income taxes (PIT) results in a total expenditure of approximately $95 million. For this reason, Tax & Rev assumes the annual aggregate cap of $10 million will be reached from FY2025 to FY2028.

Policy Issues: PIT represents a consistent source of revenue for many states. For New Mexico, PIT is approximately 25%of the state's recurring general fund revenue. While this revenue source is susceptible to economic downturns, it is also positively responsive to economic expansions. New Mexico is one of 41 states, along with the District of Columbia, that impose a broad-based PIT (New Hampshire and Washington do not tax wage and salary income). Like several states, New Mexico computes its income tax based on the federal definition of taxable income and ties to other statues in the federal tax code. This is referred to as "conformity" to the federal tax code. The PIT is an important tax policy tool that has the potential to further both horizontal equity, by ensuring the same statutes apply to all taxpayers, and vertical equity, by ensuring the tax burden is based on taxpayers' ability to pay.

The implementation of the education enrichment income tax credit will erode horizontal equity in the state income taxes. By basing the credit on qualifying dependents, taxpayers with the same level of income are no longer treated equally. Thus, two New Mexico residents who earn the same salary may have a different tax liability.

While any taxpayer with a qualifying student as a dependent may apply for this credit, most of the

[3] 2024 Poverty Guidelines Computations | ASPE (hhs.gov)

[4] AA3PM-National-Report.pdf (afterschoolalliance.org)

financial benefit is realized by middle and higher-income taxpayers. Low-income families face more obstacles when accessing out-of-school activities than higher-income families. Families must be able to initially afford the cost and out-of-school activities must be available with transportation if applicable. Also, this credit is not refundable. Lower-income families often do not have a PIT liability; thus, this credit is not beneficial to families with no tax liability. On the margin, this tax credit would allow middle income taxpayers to access additional out-of-school activities for their dependents that they may not have been able to afford previously.

Tax & Rev supports sunset dates for policymakers to review the impact of a credit before extending them. Given that this credit is new and the additional cost to the state, a sunset date would force an examination of the benefit of this credit versus the cost.

Technical Issues: The time the taxpayer has to claim the credit in Subsection D on pages 2 and 3 is currently based on 12 months from the purchase of the services. Tax & Rev suggests the 12 months should be tied to the date the certificate is issued. This is more advantageous to the taxpayer to ensure their expenditures are certified for a credit. In addition, Tax & Rev will have the certificate from the Public Education Department to administer that timeline. The requirement in Subsection G is duplicate of the language in subsection D.

Tax & Rev suggests that subsection (I)(1), on page 3, clarify whether "recreational" activities as included in the definition of "education enrichment services" include sporting activities.

Other Issues: None.

Administrative & Compliance Impact: Tax & Rev will update forms, instructions, and publications and make information system changes. Implementing the new income tax credit will be included in the annual tax year changes along with staff training to administer the credit. Tax & Rev's Administrative Services Division (ASD) will be required to test the system changes and revise revenue reports. It is anticipated this work will take approximately 40 hours, split between 2 existing full-time employees for a cost of $2,900. This bill will have a low impact on Tax & Rev's Information Technology Division (ITD), approximately 220 hours or just over 1 month and $12,210 of staff workload costs.

Estimated Additional Operating Budget Impact*				**R or NR****	**Fund(s) or Agency Affected**
FY2024	**FY2025**	**FY2026**	**3 Year Total Cost**		
--	$2.9	--	$2.9	NR	Tax & Rev – ASD staff workload
--	$12.2	--	$12.2	NR	Tax & Rev – ITD staff workload

* In thousands of dollars. Parentheses ( ) indicate a cost saving. ** Recurring (R) or Non-Recurring (NR).