F I S C A L   I M P A C T   R E P O R T

		LAST UPDATED	1/29/24
SPONSOR	Stewart	**ORIGINAL DATE**	1/28/24
SHORT TITLE	Solar Market Development Tax Credit Changes	**BILL NUMBER**	Senate Bill 121
		ANALYST	Graeser

REVENUE*
(dollars in thousands)

Type	FY24	FY25	FY26	FY27	FY28	Recurring or Nonrecurring	Fund Affected
TRD/PIT Supplemental	(2,000.0)	($14,100.0)				Nonrecurring	General Fund
TRD/PIT Regular		($18,000.0)	($18,000.0)	($18,000.0)	($18,000.0)	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	FY24	FY25	FY26	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
EMNRD	$186.8	$156.8	$156.8	$500.4	Recurring	General Fund
TRD	Minimal				Nonrecurring	General Fund

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

Relates to House Bill(s) and Senate Bill(s)

Bill ID	Title	Sponsor
HB 108	LOCAL SOLAR ACCESS FUND	Reena Szczepanski
HB 187	SCHOOL SOLAR TAX CREDIT	Joanne J. Ferrary
HB 189	LOW-INCOME SOLAR ACT	Kristina Ortez
SB 2	LOW INCOME SOLAR ACT	Carrie Hamblen
SB 121	SOLAR MARKET DEVELOPMENT TAX CREDIT CHANGES	Mimi Stewart

Sources of Information

LFC Files

<u>Agency Analysis Received From</u>
Energy, Minerals and Natural Resources Department (EMNRD)
Taxation and Revenue Department (TRD)

SUMMARY

Synopsis of Senate Bill 121

Senate Bill 121 (SB121) amends Section 7-2-18.31 NMSA 1978 in the following ways:

1) Taxpayers who install an eligible solar system on a property held by that taxpayer in leasehold from federally recognized Indian nations, tribes, or pueblos will be eligible for the tax credit;
2) Taxpayers who were eligible for the credit in tax years 2020 through 2023 but did not receive a certificate of eligibility due to the aggregate cap of available credits being reached in those tax years may apply or reapply to EMNRD for a certificate of eligibility for the qualifying solar system in tax year 2023. The aggregate cap on this supplemental opportunity is $20 million. Certificates issues pursuant to this supplemental opportunity must be claimed within 12 months of issuance, rather than the general three-year rule;
3) Increases the aggregate cap of available tax credits to $30 million annually for calendar years 2024 through 2032; and
4) Clarifies that a taxpayer who receives a certificate of eligibility from EMNRD under the special provisions for denied claims must claim their tax credit from the Taxation and Revenue Department (TRD) within 12 months following the calendar year in which the certificate was issued.

This bill does not contain an effective date and, as a result, would go into effect 90 days after the Legislature adjourns, or May 15, 2024, if enacted. A sunset date of January 1, 2032, is retained. The text of the amendment also provides sure dates for various caps and procedures.

FISCAL IMPLICATIONS

This bill expands a tax expenditure with an annual cost that is difficult to determine but likely significant. 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.

EMNRD expects the full $20 million supplemental opportunity to be used. This must be applied as a credit for the 2023 tax year and the amended tax return must be filed within 12 months of the certificate being issued by EMNRD. The effective date of the bill is May 15, 2024, and EMNRD will, for practical purposes, issue all supplemental certificates for 2020, 2021, 2022, and 2023 by the end of 2024. These supplemental certificates must be claimed on amended 2023 tax returns by December 31, 2024. For this estimate, the full amount of the $20 million supplemental cap is shown as FY25 costs.

The increase in cap amount from $12 million to $30 million – an $18 million increase – will probably phase in over a few years and probably never be exceeded. For this estimate, LFC staff assume a fiscal impact of $10 million a year (in addition to the currently allowed $12 million).

EMNRD has concerns about the cost of administering the expanded cap and expects a significant increase in the number of claims filed.

As SB121 raises the annual credit cap from $12 million to $30 million, EMNRD expects to see a commensurate increase in applications for certificates. Furthermore, the $20 million ‘lookback’ provision in SB121 will create a one-year-long spike in applications which will require additional staff resources. Thus, EMNRD would need 2 new FTEs (including salary and benefits) to administer the program, including processing the additional applications received. These two new FTE are currently in the executive recommendation for HB2.

EMNRD will also require approximately $30 thousand in one-time costs for program updates, and administrative, legal and information technology staff time to update the electronic application process. Staff are necessary to effectively manage the program, provide system reviews, certify systems for tax credit eligibility, collect data, and maintain the required databases.

TRD expects the increases in cap amount to stabilize at the maximum amount provided:

Estimated Revenue Impact*					R or NR**	Fund(s) Affected
FY24	FY25	FY26	FY27	FY28		
($2,000.0)	($32,100.0)	($18,000.0)	($18,000.0)	($18,000.0)	R	General Fund

The average cost per watt for installing a residential solar panel system in New Mexico ranges from $2.79 to $3.77, excluding federal solar tax credits and other rebates[1]. Commercial solar PV projects typically have a lower cost per watt due to economies of scale. The average payback period for a residential system is 10.2 years, and the typical lifespan of solar projects is around 30 years, providing homeowners with decades of "free" solar power.

In the past decade, the solar industry in the United States has experienced remarkable growth, boasting an average annual rate of 24 percent[2]. This growth resulted in the total solar capacity exceeding 110 gigawatts in 2022. Notably, solar energy accounted for 45 percent of the new electricity-generating capacity additions in the country during the same year. Of the overall solar capacity installed in the U.S., more than 20 percent can be attributed to residential installations. This segment has witnessed significant expansion in recent years, with approximately 3.6 million installations recorded in 2022. In New Mexico, the credit cap of $12 million was reached in FY2022 and FY2023. The Taxation and Revenue Department (TRD) assumed a consumer demand of $17 million in tax credits in tax year 2022 given the $12 million certification cap was reached and the need to extend $20 million in additional credits for calendar years 2020 to 2023. TRD projected that New Mexico would experience a similar growth rate in the solar market, consistent with the national average of 24 percent and thereby hit the new $30 million certification cap in tax year 2025. The fiscal impact is the difference between the current cap of $12 million and the new cap of $30 million.

The additional $20 million of credits for the prior years of 2020 through 2023 must be claimed for taxable year 2023. As noted in “Other Issues” below, taxpayers will begin to file their 2023 tax returns this January and may need to amend the return at a later date. The effective date of May 15, 2024, means applications for the credit and tax returns with the

[1] A Quick Guide To IRS Form 5695 (greenlancer.com)

[2] Residential solar market in the U.S. - statistics & facts | Statista

credit cannot occur until that time. TRD assumes that $2 million in credits from the $20 million will impact FY24 and the remaining will impact FY25. However, the alternative would be for taxpayers who were denied the credit in prior years due to the cap being reached to claim the credit for taxable year 2024; in that case, they would not receive the relief until filing in early 2025, an undesirable delay.

SIGNIFICANT ISSUES

EMNRD has provided extensive data and perspectives on the Solar Market Development Tax Credit:

Benefits of the New Solar Market Development Tax Credit

The New Solar Market Development Tax Credit has been incredibly popular amongst New Mexicans, creating a vibrant solar industry and reducing greenhouse gas emissions from the power sector in New Mexico. Since the inception of the credit in 2020, more than 12,202 taxpayers have used it to help them defray the cost of installing residential solar systems. The average taxpayer is saving 13,522 kWh of energy and $1,623 per year on their electric bills. A total of 97.06 MW of electricity generation capacity has been added to distribution systems of utilities of New Mexico, reducing the state's CO2 emission by 70,122 tons.

Furthermore, all these solar systems purchased by New Mexicans have cost $144.5 million, with installation labor of an additional $42.6 million, increasing economic activity in New Mexico by over $187.1 million per year.

The non-profit Solar Energy Industries Association and DOE's National Renewable Energy Laboratory estimate the tax credit has created the following New Mexican jobs:

Estimated Jobs Supported by the New Solar Market Development Tax Credit				
	2020	2021	2022	2023
Total Jobs Created (SEIA estimate)	493	543	787	713
Total Jobs Created (NREL estimate)	559	616	893	809

Provisions added to the credit in recent legislative sessions, like refundability and transferability, have helped lower-income New Mexicans access residential solar as well.

Oversubscription and SB121's Cap Increase and Lookback Provisions

However, the credit's popularity has created constant issues with oversubscription, exhaustion of the annual aggregate cap, and commensurate rejection of otherwise perfectly eligible applications – disappointing New Mexicans and creating financial difficulties for those who had counted on the tax credit to defray their solar costs. The yearly aggregate cap is usually met three to five months before the end of a tax year.

EMNRD's informal records show that at least 849 applications could not be funded in 2021 and 2022 combined. From 2020 to 2023, issued credits surged 43 percent. It is likely that the current $12 million fund cap will be exceeded in 2023 and future years. EMNRD estimates at least 500 additional applications for the 2023 tax year will be rejected due to exhaustion of the cap. These numbers are estimates, as EMNRD has no visibility into the total number of taxpayers who could have, but did not, attempt to receive a tax credit after the yearly cap had been reached – only the number who were rejected by the agency.

Funding History

Year	Application Count	Issued	Fund Cap	Status
2020	2369	$ 6,695,238	$ 8,000,000	Qualification Period Elapsed
2021	2613	$ 8,000,000	$ 8,000,000	Exhausted Fund
2022	3785	$12,000,000	$ 12,000,000	Exhausted Fund
2023	3396	$10,779,966	$ 12,000,000	On Target to Exhaust March 2024
2024	3	$ 7,618	$ 12,000,000	Started issuing

The following table demonstrates EMNRD's best guess at the required funding necessary to 'make whole' known rejected applicants from 2021 and 2022. 2023 applicants are not yet reflected in this table.

Rejected NSMDTC Applications Due to Exhausted Fund Estimated Amount to Make Whole			
Application Source	**Count**	**Average**	**Estimated**
2021 Electronic	42	3,062	128,604
2021 Paper	442	3,062	1,353,404
2022 Electronic	41	3,168	129,888
2022 Paper	324	3,168	1,026,432
	849	Total	2,638,328

The table below shows the percentage of applications which were rejected solely based on the yearly cap being expended and would have otherwise been approved.

Year	Rejected	Issued	Sum	% not approved
2021	484	2613	3097	16%
2022	365	3785	4150	9%
2023	estimated 500	current 4448	4948	10.11%

In addition, EMNRD has received information from the Public Service Company of New Mexico (PNM) regarding the number of residential solar interconnection applications they have received in tax year 2023. To date, PNM has received 6,444 applications, and interconnected 6,024 of them. If all 6,024 applicants applied for the Solar Market Development Tax Credit, the total tax liability necessary to meet demand – in just this one service area – would be $18,258,744. So far in 2023, EMNRD has approved nearly 5,000 applications, and only approximately $1 million remains in the 2023 cap. We therefore expect that the cap will be exceeded by at least 1,000, if not many more applications, especially considering those taxpayers outside the PNM service area that may also apply.

Raising the aggregate cap to $30 million in tax years 2024-2032, as SB121 does, will likely eliminate the problem of oversubscription. In addition, creating the $20 million 'lookback' provision in tax year 2023 will go a long way – perhaps even all the way – to addressing those taxpayers who applied and were rejected for certificates due to the exhaustion of the cap.

Tribal Eligibility Provisions

The statute authorizing the New Solar Market Development Tax Credit inadvertently made certain New Mexicans, namely those who hold leasehold properties on federally recognized nations, tribes, and pueblos in New Mexico, ineligible for the credit. As written the language in the Act only made the credit available to structures "owned by that taxpayer." The convention for ownership on tribal and pueblo land is that a homeowner may purchase a structure but that the land underneath is held in trust by the tribe or pueblo. This made certification of systems impossible. The provisions in SB121 fix this unintentional exclusion.

TRD provides additional commentary on policy issues:

Personal income tax (PIT) represents a consistent source of revenue for many states. For New Mexico, PIT is approximately 25 percent 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). 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. This solar market incentive erodes horizontal equity as this is only eligible to taxpayers who own a home or business and can afford the investment of a solar system.

The inclusion of a residence or business owned by a federally recognized Indian nation, tribe or pueblo increases horizontal equity by increasing the number of taxpayers eligible to claim the credit. The current version of the credit requires proof that a residential solar installation is owned by the taxpayer. This requirement inadvertently left out residences on tribal trust land, and this bill corrects that issue.

The broader question of subsidizing solar energy has many economic factors to consider including job creation, impacts to established markets and environmental concerns. A credit is a tax expenditure that gives preferential tax treatment to certain taxpayers. Some economists would argue that energy costs should reflect the associated cost impacts or benefits to the environment. Thus, solar energy which can be expensive to start-up, should be given tax incentives due to its low environmental impact and health and social benefits for the current and future populations. The long-term environmental, health and social benefits outweigh the short-term revenue cost. New job opportunities are associated with solar energy generation, such as solar photovoltaic installers, engineers and managers.

Credit applications being denied in prior years only as a result of the credit certification cap being reached has been a frustrating experience for taxpayers. This bill will allow individuals who purchased a system prior to tax year 2024, under the impression that they would get a state credit for their purchase, to be made whole.

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.

EMNRD comments on performance:

> To develop and implement the revised rules required by the new provisions in SB121, EMNRD will need additional legal and administrative resources. In addition, IT services – either internal, contractual or both – will be needed to continue to improve and update the online application process. Furthermore, without the 2 FTEs in the executive recommendation, EMNRD may not be able to process the increased number of applications in a rapid and secure fashion.

ADMINISTRATIVE IMPLICATIONS

EMNRD will need to develop and maintain data to report to the legislature and to TRD; to revise and update the existing Solar Market Development Tax Credit rules to implement the changes in SB121; to update the electronic submission portal in anticipation of the increased volume of applications; and provide technical assistance to guide applicants through the electronic portal application process. In 2021 and 2022, over 784 applications were submitted in paper form; these applicants will need to update their applications to digital form if they apply for the 'lookback' provision.

	FY24	FY25	FY26	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
Staff	156.8	156.8	156.8	470.4	Recurring	GF
Contracts	30.0	00	0	30.0	Recurring	GF

TRD will make information system changes and update forms, instructions, and publications. These changes will be included in annual tax year changes.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

The following bills this session deal with various aspects of encouraging solar development:

Bill ID	Title	Sponsor
HB 108	LOCAL SOLAR ACCESS FUND	Reena Szczepanski
HB 187	SCHOOL SOLAR TAX CREDIT	Joanne J. Ferrary
HB 189	LOW-INCOME SOLAR ACT	Kristina Ortez
SB 2	LOW INCOME SOLAR ACT	Carrie Hamblen
SB 121	SOLAR MARKET DEVELOPMENT TAX CREDIT CHANGES	Mimi Stewart

TECHNICAL ISSUES

TRD points out a needed clarification:

> The additional caps in subsection F(1), on page 4, need clarification, as it is unclear whether the additional $20 million applies to each tax year listed (2020 through 2023) or if it pertains to the total for all the years mentioned. TRD understands the intent of the bill is for $20 million to be made available in total, not $20 million for each fiscal year for $80 million in total. But without clarification, if the $20 million intended is received, taxpayers may dispute credit denials.

In addition, TRD suggests the following instruction be added:

To enhance process efficiency and reduce internal risk, TRD suggests inserting the following text on page 3, line 18, immediately after the word "claimed": "The Energy Minerals and Natural Resources Department shall regularly provide the department with electronically issued certificates of eligibility at agreed-upon intervals."

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 Principles	Met?	Comments
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.	✓	
Targeted: 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	 ✓ ✓ ✓	The state has taken an experimental approach to the appropriate limit – sufficient to encourage the development of the industry but with nothing unutilized.
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. Public analysis 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. Fulfills stated purpose Passes "but for" test	 ✓ ?	The combination of a federal 30% credit with this 10% credit has been quite effective in developing the industry.
Efficient: The tax expenditure is the most cost-effective way to achieve the desired results.	?	
Key: ✓ Met ✗ Not Met ? Unclear		

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