FISCAL IMPACT REPORT

LAST UPDATED
SPONSOR Borrego/Martinez, J **ORIGINAL DATE** 2/1/24
SHORT TITLE Home Fire Recovery Tax Credit **BILL NUMBER** House Bill 10

ANALYST Torres, Ismael

REVENUE*
(dollars in thousands)

Type	FY24	FY25	FY26	FY27	FY28	Recurring or Nonrecurring	Fund Affected
PIT/CIT		($18,900.0) to ($105,000.0)	($18,900.0) to ($105,000.0)	($18,900.0) to ($105,000.0)	($18,900.0) to ($105,000.0)	Recurring	General Fund

Parentheses ( ) indicate revenue decreases.
*Estimates on the impacts of this bill are particularly difficult to discern. Numbers provided are intended to illustrate a potential magnitude of impact and not an exact amount. Please see Fiscal Implications for more information..

Sources of Information

LFC Files

Agency Analysis Received From
New Mexico Attorney General (NMAG)

SUMMARY

Synopsis of House Bill 10

House Bill 10 (HB10) would establish an income tax credit for taxpayers whose homes were destroyed in a wildfire between 2021 and 2023. The tax credit is equal to the full amount of the construction costs of qualified, permanently constructed homes and can be used against taxpayer's tax liability for up to three years. Qualified site-built homes are defined to be those constructed on the same property as the destroyed home less any compensation received pursuant to the federal Hermit's Peak/Calf Canyon Fire Assistance Act, though application for those funds is not required to receive state assistance.

The construction industry division would promulgate rules and forms to quality people for the tax credit.

The credit is applicable beginning in tax year 2024.

FISCAL IMPLICATIONS

This bill creates a tax expenditure with a 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. 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.

The table on page one presents an estimate of potential impacts intended to illustrate a magnitude rather than an exact amount. To gauge potential impacts, LFC staff utilized data from FEMA, local builders and realtors, and published estimates of homes lost to wildfires in 2021-2023.

The latest report estimates 430 homes were destroyed in the hermit's peak/calf canyon fires[1], though estimates range as high as 500. Over 200 homes were reported to be destroyed by the McBride Fire. The bill would also include any other fires that destroyed homes during the allowable period. In a small survey of builders and realtors, LFC staff were quoted construction costs between $200 a square foot to $300 a square foot.

For the lower end of the cost estimate, assumptions of $200 per square foot and a home size of 1,500 square feet were used, plus a 90 percent federal reimbursement rate and low tax liabilities. The upper end of the estimate assumed 700 homes with a cost estimate of $300 per square foot and 2,000 square feet of construction per home with no assumptions on federal reimbursement or tax liability. Given those factors, construction costs could be between $ million and income tax credits could equal that amount. Those figures are spread over the likely time frame on page 1.

Risks to the Estimate

There is significant uncertainty in the application of this bill that makes it difficult to determine if the actual costs would be higher or lower than these estimates.

First, it is unknown how much federal assistance will offset the cost of this credit. The bill does *not* require taxpayers to seek funds from insurance or federal sources to reduce the cost of the credit. Further, taxpayers are frequently rejected or delayed in receiving Federal Emergency Management Agency funds[2] and could seek state resources despite the availability of federal support.

Second, the credit does not limit construction costs, the size of the home, or other valuation limits which could incentivize the construction of homes worth and costing higher than the home being replaced or median values. This would likely result in homes much more costly than estimated here, which would equally increase the cost to the state for this credit.

Third, taxpayers typically have insufficient tax liabilities for the full cost of construction to apply as a credit against their tax liability. That would mean the cost could be less than presented here. However, increased tax liabilities may exist for taxpayers receiving income-based compensation from federal assistance. Should taxpayers receive large income-based payouts that increase state tax liability, tax credit costs could rise as the credit is taken against a larger liability. Furthermore, the credit also applies to business income which complicates estimation and could

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[1] https://www.propublica.org/article/after-hermits-peak-calf-canyon-wildfire-quantifying-victims-suffering-becomes-legal-battle

[2] https://www.npr.org/transcripts/1143929966

increase the cost if those credits were applied to larger liabilities under business entities.
Fourth, the timing of payments is highly unpredictable. Impacts could begin in FY25 or sooner if houses have already been completed.

Finally, federal assistance is "limited to actual compensatory damages"[3] and not replacement value of a newly constructed home. Therefore, if taxpayers choose to construct homes greater in cost than the value of the home lost, the entirety of the higher cost would be credited against taxpayer's state tax liabilities. Because of the incentive created, costs could be higher than estimated here.

SIGNIFICANT ISSUES

The 2022 fire season was one of New Mexico's worst, with both the largest wildfire—Calf Canyon/Hermit's Peak—and second largest wildfire—Black—in state history. While the Black Fire in the Gila National Forest primarily impacted wilderness, hundreds of houses were lost in the Calf Canyon fire northwest of Las Vegas and the McBride fire east of Ruidoso. HB10 is intended to compensate the homeowners affected but, given the availability of federal compensation and the socioeconomic demographics of the regions affected, it is difficult to predict whether and how those homeowners will access the benefit.

Uptake. The U.S. Census Bureau sets the average household income in San Miguel County at $43.5 thousand, over $15 thousand less than the state average of $58.7 thousand, and it is difficult to predict whether lower income homeowners would be able to secure the upfront financing to rebuild their homes and take advantage of the tax credit. Further, the tax burden on these lower income homeowners might not be sufficient to make the tax credit of much value.

Potential for Loss of Federal Assistance. Delays in being able to access federal funds for Calf Canyon Fire losses has led to two lawsuits against FEMA. Any federal compensation for home loss would be deducted from the tax credit, but should accessing federal assistance continue to be burdensome and slow, some residents might forgo federal assistance, knowing they can claim a full credit against their state taxes. In effect, this would mean state dollars were supplanting federal dollars.

Construction Costs. Should the credit from HB10 prove popular, it could indirectly trigger high construction demand and higher construction costs. This could drive up housing costs in a region with a population that is poorer than the state average.

Incentive for Overbuilding. While the tax credit might prove unattractive to lower income homeowners, the credit, which is not limited to the value of the lost home, could encourage those with greater means to seek high-cost replacements. Those households, with higher tax burden, are also more likely to be attracted to the tax credit.

OTHER SUBSTANTIVE ISSUES

In assessing all tax legislation, LFC staff considers whether the proposal is aligned with

[3] FEMA Legal Analysis of Noneconomic Damages, http://bit.ly/3SpBNmZ

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.

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