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FISCAL IMPACT REPORT

ORIGINAL DATE 02/18/21

SPONSOR Munoz LAST UPDATED _____ HB _____

SHORT TITLE Retention of Funding by Municipalities SB 226

ANALYST Iglesias

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY21	FY22	FY23	FY24	FY25		
-	(\$2,548.4)	(\$3,149.7)	(\$3,776.4)	(\$4,434.1)	Recurring	General Fund
-	\$2,548.4	\$3,149.7	\$3,776.4	\$4,434.1	Recurring	Five Municipalities

Parenthesis () indicate revenue decreases

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

FY21	FY22	FY23	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
\$10.3	-	-	\$10.3	Nonrecurring	TRD – ITD Staff General Fund

Parenthesis () indicate expenditure decreases

SOURCES OF INFORMATION

LFC Files

Responses Received From

Taxation and Revenue Department (TRD)

Department of Finance and Administration (DFA)

SUMMARY

Synopsis of Bill

Senate Bill 226 amends Sections 7-1-6.46 and 7-1-6.47 NMSA 1978, which provide for distributions to municipalities and counties, respectively, to offset losses from the food and health care practitioner services deductions allowed for gross receipts tax (GRT) under Sections 7-9-92 and 7-9-93 NMSA 1978 (commonly known as “hold harmless” distributions).

Specifically, the bill creates a new set of municipalities (those with populations between 10 thousand and 25 thousand) to receive a larger hold harmless distribution than other local governments subject to the existing phase out. This bill would allow these municipalities to continue to receive into perpetuity a distribution equal to 90 percent of the GRT that would have

otherwise been generated from food and healthcare practitioner services.¹

The bill also creates a cut-off of June 30, 2019 for determining if a county or municipality did not have a hold harmless gross receipts tax ordinance in effect, for the purpose of determining the amount of distribution a municipality or a county could receive. This change is primarily clean-up since the hold harmless increments were repealed and consolidated into the unrestricted local option rate under Laws 2019, Chapter 274 (HB 479).

The bill also simplifies language in Sections 7-1-6.46 and 7-1-6.47 NMSA 1978. “Maximum distribution” is also defined differently based on when the hold harmless gross receipts tax ordinance was in effect.

Lastly, the bill adds a full phase-out of hold harmless distributions, equaling the distributions for certain local governments to zero in FY30, whereas current law only phases out to 7 percent in FY29.

The effective date of this bill is July 1, 2021.

FISCAL IMPLICATIONS

The bill bases the eligibility of the 90 percent hold harmless distribution on the population data according to the most recent decennial census. Currently, that would be the 2010 census, but by the bill’s effective date, it would be based on the 2020 census.

LFC staff used 2019 population estimates from the U.S. Census Bureau to estimate which municipalities would qualify based on the 2020 census. Based on this 2019 data, four municipalities (Gallup, Las Vegas, Los Lunas, and Portales) would be eligible to receive the 90 percent hold harmless distribution. Notably, the official census count could change which municipalities are eligible – for example, under the 2010 census, Silver City would be also eligible, which would increase the cost of the bill. See Attachment 1 for a comparison of 2010 census data versus the 2019 population estimate.

Under current law, these municipalities would have received a declining percentage of hold harmless distributions through 2029. Under this bill, these municipalities would receive a constant distribution equal to 90 percent of the lost revenues into perpetuity. Therefore, the cost of this provision increases over time, as demonstrated in the fiscal impact table, totaling about \$2.5 million in FY21 and increasing to \$4.4 million in FY25.

This bill may be counter to the LFC tax policy principle of adequacy, efficiency, and equity. Due to the increasing cost of tax expenditures, revenues may be insufficient to cover growing recurring appropriations.

SIGNIFICANT ISSUES

In 2004, the GRT was removed from food for home consumption and medical services by enacting

¹ Under current law, for municipalities with populations greater than 10 thousand and counties with populations greater than 48 thousand, the hold harmless distributions phase out, with distributions at 63 percent in FY21 and gradually reducing to 7 percent by 2030.

two GRT deductions. Local governments were given new authority to enact up to 3/8 percent in new local option hold harmless GRT increments. Hold harmless distributions from the state to local governments were enacted so that the state would bear the entire cost of the two deductions. With the rising cost of both the deductions and the hold harmless payments, the 2013 Legislature enacted legislation that phases-out the food and medical hold harmless payments to local governments to 7 percent by FY29. The 2013 legislation made an exception to the hold harmless phase-out for municipalities with a population under 10,000 and counties under 48,000 that had not imposed a GRT hold harmless increment. Smaller local governments are often more vulnerable to significant swings in revenues. The food and medical hold harmless payments provide a stable tax base for smaller local governments, and as a result the Legislature ensured that they retained this revenue stream.

The proposed change would result in the exemption of four additional municipalities that had not elected to impose hold harmless GRT increments prior to June 30, 2019 from the food and medical hold harmless phase-out, and set their distribution at 90 percent of the total maximum distribution. The bill would also fully phase-out hold harmless distributions for larger local governments to 0 percent in FY30. This would keep a subset of municipalities that are slightly larger in population than the original exempted group of municipalities, with populations less than 10,000, nearly whole.

Municipalities with a population of 10,000 or more but less than 25,000 are still relatively small and may not have a broad enough economic base to support local government operations without the stability and size of food and medical tax revenues. This bill would provide revenue stability and assist in the financial health of the municipalities addressed in the legislation. These five municipalities are in general falling behind in GRT revenue compared to their counterparts who enacted a hold harmless gross receipts tax increment. Thus, the additional distribution amount can be seen as putting them financially at par with other relative sized counterparts. However, this relationship changes each year as the phase-out gets closer to 0 percent for those that did enact.

Based on the 2020 Tax Expenditure Report, in Fiscal Year 2020, state general fund revenue was reduced by \$252.7 million as a result of the food deduction, and by another \$142.9 million as a result of hold harmless distributions to local governments. Local government revenue was reduced by \$61.2 million. Similarly, in Fiscal Year 2020, state general fund revenue was reduced by \$37.1 million as a result of the medical services deduction, and by another \$19.5 million as a result of hold harmless distributions to local governments. Local government revenue was reduced by \$8.4 million as a result of the medical services deduction.

Under current law, the small city and county exclusion from the phase out is estimated to have resulted in additional general fund costs of about \$6.6 million in FY20. The ongoing cost of this exclusion from the phase out is estimated to result in an ongoing cost of about \$23 million per year by FY30. This bill would add to that ongoing cost of hold harmless distributions to local governments exempt from the phase out.

By fully phasing out the hold harmless distributions for larger cities and counties in FY30, this bill will save the general fund about \$6 million per year starting in FY30, at an equal cost to affected local governments.

ADMINISTRATIVE IMPLICATIONS

The Taxation and Revenue Department states the Information and Technology Division (ITD) of TRD estimates that implementation of the legislation will cost approximately \$10.3 thousand in staff workload.

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

ATTACHMENT 1

Annual Estimates of the Resident Population for Counties in New Mexico: April 1, 2010 to July 1, 2019		
Geographic Area	Census	2019 est.
Bernalillo County	662,564	679,121
Catron County	3,725	3,527
Chaves County	65,645	64,615
Cibola County	27,213	26,675
Colfax County	13,750	11,941
Curry County	48,376	48,954
De Baca County	2,022	1,748
Doña Ana County	209,233	218,195
Eddy County	53,829	58,460
Grant County	29,514	26,998
Guadalupe County	4,687	4,300
Harding County	695	625
Hidalgo County	4,894	4,198
Lea County	64,727	71,070
Lincoln County	20,497	19,572
Los Alamos County	17,950	19,369
Luna County	25,095	23,709
McKinley County	71,492	71,367
Mora County	4,881	4,521
Otero County	63,797	67,490
Quay County	9,041	8,253
Rio Arriba County	40,246	38,921
Roosevelt County	19,846	18,500
Sandoval County	131,561	146,748
San Juan County	130,044	123,958
San Miguel County	29,393	27,277
Santa Fe County	144,170	150,358
Sierra County	11,988	10,791
Socorro County	17,866	16,637
Taos County	32,937	32,723
Torrance County	16,383	15,461
Union County	4,549	4,059
Valencia County	76,569	76,688
<p>Note: The estimates are based on the 2010 Census and reflect changes to the April 1, 2010 population due to the Count Question Resolution program and geographic program revisions. All geographic boundaries for the 2019 population estimates are as of January 1, 2019. For population estimates methodology statements, see http://www.census.gov/programs-surveys/popest/technical-documentation/methodology.html.</p>		
<p>Annual Estimates of the Resident Population for Counties in New Mexico: April 1, 2010 to July 1, 2019 (CO-EST2019-ANNRES-35)</p> <p>Source: U.S. Census Bureau, Population Division</p> <p>Release Date: March 2020</p>		

Annual Estimates of the Resident Population for Incorporated Places in New Mexico: April 1, 2010 to July 1, 2019

Geographic Area	Census	2019	Geographic Area	Census	2019
Alamogordo city	30,403	31,980	Lake Arthur town	436	420
Albuquerque city	545,852	560,513	Las Cruces city	97,618	103,432
Angel Fire village	1,216	1,070	Las Vegas city	13,753	12,919
Anthony city	(X)	9,239	Logan village	1,042	979
Artesia city	11,301	12,356	Lordsburg city	2,797	2,398
Aztec city	6,763	6,369	Los Lunas village	14,835	16,061
Bayard city	2,328	2,123	Los Ranchos de Albuquerque village	6,024	6,108
Belen city	7,269	7,416	Loving village	1,413	1,393
Bernalillo town	8,320	10,477	Lovington city	11,009	11,489
Bloomfield city	8,112	7,685	Magdalena village	938	878
Bosque Farms village	3,904	3,888	Maxwell village	254	212
Capitan village	1,489	1,431	Melrose village	651	629
Carlsbad city	26,138	29,810	Mesilla town	2,196	1,828
Carrizozo town	996	935	Milan village	3,245	3,669
Causey village	104	98	Moriarty city	1,910	1,860
Chama village	1,022	992	Mosquero village	93	85
Cimarron village	1,021	881	Mountainair town	928	873
Clayton town	2,980	2,681	Pecos village	1,392	1,320
Cloudcroft village	674	701	Peralta town	3,660	3,584
Clovis city	37,775	38,319	Portales city	12,280	11,610
Columbus village	1,664	1,617	Questa village	1,770	1,755
Corona village	172	163	Raton city	6,885	5,938
Corrales village	8,329	8,696	Red River town	477	463
Cuba village	731	757	Reserve village	289	277
Deming city	14,855	13,880	Rio Communities city	(X)	4,552
Des Moines village	143	122	Rio Rancho city	87,521	99,178
Dexter town	1,266	1,243	Roswell city	48,366	47,551
Dora village	133	121	Roy village	234	211
Eagle Nest village	290	251	Ruidoso village	8,029	7,901
Edgewood town	3,735	6,107	Ruidoso Downs city	2,815	2,574
Elephant Butte city	1,431	1,310	San Jon village	216	202
Elida town	197	176	Santa Clara village	1,686	1,761
Encino village	82	78	Santa Fe city	67,947	84,683
Española city	10,224	10,044	Santa Rosa city	2,848	2,636
Estancia town	1,655	1,571	San Ysidro village	193	201
Eunice city	2,922	3,038	Silver City town	10,315	9,386
Farmington city	45,877	44,372	Socorro city	9,051	8,348
Floyd village	133	110	Springer town	1,047	906
Folsom village	56	57	Sunland Park city	14,106	17,978
Fort Sumner village	1,031	897	Taos town	5,716	5,929
Gallup city	21,678	21,493	Taos Ski Valley village	69	71
Grady village	107	103	Tatum town	798	829
Grants city	9,182	8,942	Texico city	1,130	1,067
Grenville village	38	29	Tijeras village	541	535
Hagerman town	1,257	1,220	Truth or Consequences city	6,475	5,753
Hatch village	1,648	1,650	Tucumcari city	5,363	4,867
Hobbs city	34,122	39,141	Tularosa village	2,842	3,006
Hope village	105	106	Vaughn town	446	397
House village	68	62	Virden village	152	129
Hurley town	1,297	1,176	Wagon Mound village	314	287
Jal city	2,047	2,117	Willard village	253	242
Jemez Springs village	250	267	Williamsburg village	449	408
Kirtland town	(X)	601			

Note: The estimates are based on the 2010 Census and reflect changes to the April 1, 2010 population due to the Count Question Resolution program and geographic program revisions. All geographic boundaries for the 2019 population estimates are as of January 1, 2019. An "(X)" in the 2010 Census field indicates a locality that was formed or incorporated after the 2010 Census. Additional information on these localities can be found in the Geographic Boundary Change Notes (see <https://www.census.gov/programs-surveys/geography/technical-documentation/boundary-change-notes.html>). For population estimates methodology statements, see <http://www.census.gov/programs-surveys/popest/technical-documentation/methodology.html>.

Annual Estimates of the Resident Population for Incorporated Places in New Mexico: April 1, 2010 to July 1, 2019 (SUB-IP-EST2019-ANNRES-35)

Source: U.S. Census Bureau, Population Division

Release Date: May 2020