TAXATION & REVENUE
NEW MEXICO

New Mexico 2023
Tax Expenditure Report

Presented to the
Revenue Stabilization and Tax Policy Committee

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What is a Tax Expenditure Report?

- Tax expenditure reports (TER) describe areas where the tax code provides for preferential tax treatment of a certain activity
- The TER includes an estimate of revenue foregone because of the preferential tax treatment due to:
  - Credits
  - Deductions
  - Exemptions
  - Preferential tax rates
- Every dollar of revenue foregone is a dollar that cannot be appropriated or added to reserves
- State appropriations are rigorously evaluated and reprioritized annually; tax expenditures should be similarly revisited
- TERs are important transparency tools that allow State policymakers, advocacy groups, and the public an opportunity to regularly evaluate the State's tax code

New Mexico's Tax Expenditure Report

- An annual TER has been produced by Tax & Rev since 2012
- 2023 legislation now requires TER in statute (7-1-84 NMSA 1978)
- Format has evolved over time
  - Separately identifies each "deviation" from the tax base
  - Categorizes each deviation as a tax expenditure, non tax expenditure, or "arguable"
  - Provides a description of each expenditure, the statutory reference, purpose, amendment history, estimated cost, evaluation, and recommendations
  - Tax & Rev constantly seeks to improve cost estimates
  - Categorizes each expenditure as existing for citizen benefit, economic development, environment, highly-specialized industries, or health care
- Reports can be found at www.tax.newmexico.gov, then under Forms & Publications, Publications, Tax Expenditure Reports

What are the Differences? Exclusions

- Exclusions – amounts of gross receipts, gross income, or other amount that is removed <u>to define the tax base</u>
  - Taxpayers exclude certain amounts of their “base income” to derive “net income” on which tax is imposed. § 7-2-2(N)
  - The property tax excludes personal property and has a 3% limit on annual value growth on residential property
  - For gross receipts tax, taxpayers exclude certain amounts to derive their “gross receipts” on which tax is imposed

What are the Differences? Exemptions

- Exemptions – usually eliminate a taxpayer's obligation to register, report, and pay tax
- Tax & Rev does not have visibility into income or receipts that are exempt because they are not reported on a tax return
- Exemptions can hinge on the nature or character of the taxpayer. For example:
  - Insurance companies are exempt from CIT because they pay premium tax
  - Nonprofits and disabled street vendors are exempt from GRT
  - Active-duty armed forces salaries and persons over 100 years of age are exempt from PIT
  - Certain disabled military veterans are exempt from motor vehicle excise tax
- Exemptions can hinge on the nature of the transaction. For example:
  - Commercial vehicles operating within 10 miles of the Mexico border are exempt from weight distance tax and trip tax
  - Receipts from sale and use of vehicles on which motor vehicle excise tax is imposed are exempt from GRT and compensating tax
- Generally, if the exemption is full and applies to the nature of the taxpayer, or if a taxpayer solely engages in exempt transactions, there is no registration or filing obligation

What are the Differences? Deductions

- Deductions - reduce tax liability by making certain transactions or income reported on returns deductible from taxable receipts/income
- Deductions and exemptions have the same effect on a taxpayer's tax liability, but differ in taxpayer reporting obligations
- Deductions lower the tax base before calculating tax due
  - For GRT, taxpayers report a gross amount of receipts, then subtract the amount of the receipts that are deductible to compute taxable gross receipts
  - Some deductions are combined on a return; others are separately reported
  - Many GRT deductions statutorily require the seller to be in possession of a Nontaxable Transaction Certificate (NTTC) or alternative evidence at the time the return is due for the receipts from the transactions or within sixty days of a Tax & Rev audit notice
- Examples
  - Back-to-School Tax-Free Weekend GRT receipts deduction
  - 40% capital gains deduction from PIT
  - Food for home consumption GRT deduction
  - Health care practitioner services GRT deduction
  - Sale of prosthetic devices GRT deduction

What are the Differences? Credits

- Credits – reduce a taxpayer's tax liability dollar for dollar
  - Many credits require an application for approval to either Tax & Rev or another certifying agency before the credit is allowed
  - Where deductions and exemptions apply to one tax program, credits can offset tax liabilities across several tax programs
  - Some credits can be transferrable
  - Some credits can be refundable or carried forward to future tax years if the amount of the credit exceeds the taxpayer's tax liability
  - Examples:
    - Working families tax credit for PIT
    - Angel investment PIT credit
    - Child care to prevent indigency PIT credit
    - Film tax credit against CIT and PIT
    - High-wage jobs credit against modified combined tax
    - Investment credit against GRT, Comp Tax, Withholding
    - Rural health practitioner PIT credit

Baseline System of Taxation

- Any tax program or baseline system of taxation is the application of a "tax rate" multiplied by a "tax base"
  - Common tax bases for New Mexico tax programs:
    - "Gross receipts" from sales of property or services or the "purchase value" of property (GRT/Comp)
    - "Net income" (CIT/PIT)
    - "Taxable value" (Severance-related taxes)
    - A percentage of "fair market value" for locally assessed property taxes
  - "Tax rate" is simply a percentage applied to the tax base

Tax Expenditures Must be a Deviation from the Tax Base

- Exclusions to derive the tax base are not considered deviations and are not considered tax expenditures
- Deviations can occur for many reasons:
  - “In lieu of” taxation
  - US constitutional prohibition or federal pre-emption
  - Government-to-government comity
  - To “true” a tax base – anti-pyramiding, bad debts
  - To provide special or preferential treatment to achieve a policy objective

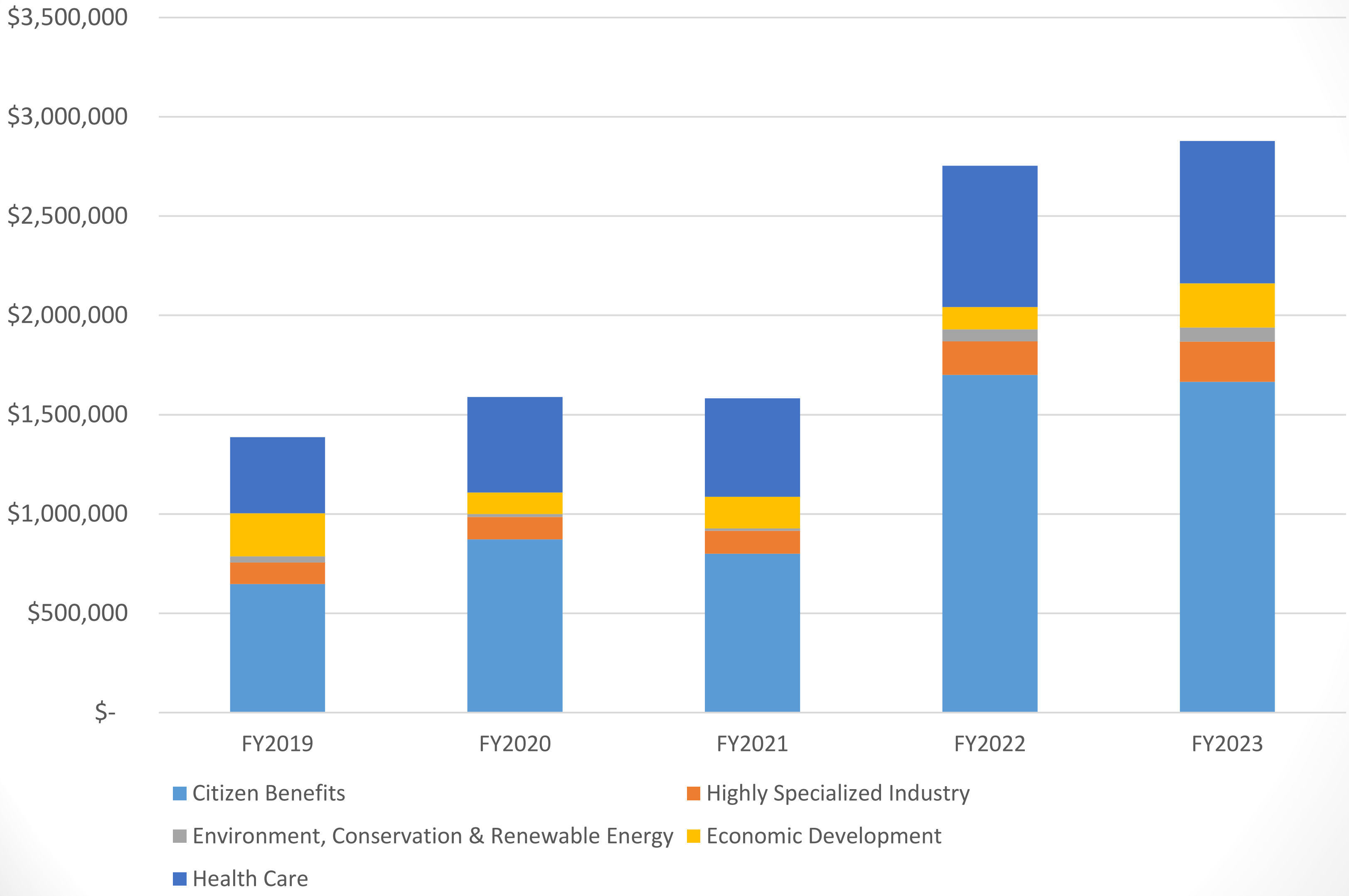
Tax Expenditures Must Convey Special Treatment

- Special treatment is typically evidenced by a policy choice regarding:
  - Benefitting a subset of the tax base
  - Benefitting a subset of the population or
  - Both
- Policy choices:
  - To benefit all, or a specific subset, of citizens
  - To induce economic development
  - To induce conservation
  - To aid specific industries
  - To encourage or discourage certain behaviors or activities, particularly related to health

Tax Expenditure Categories

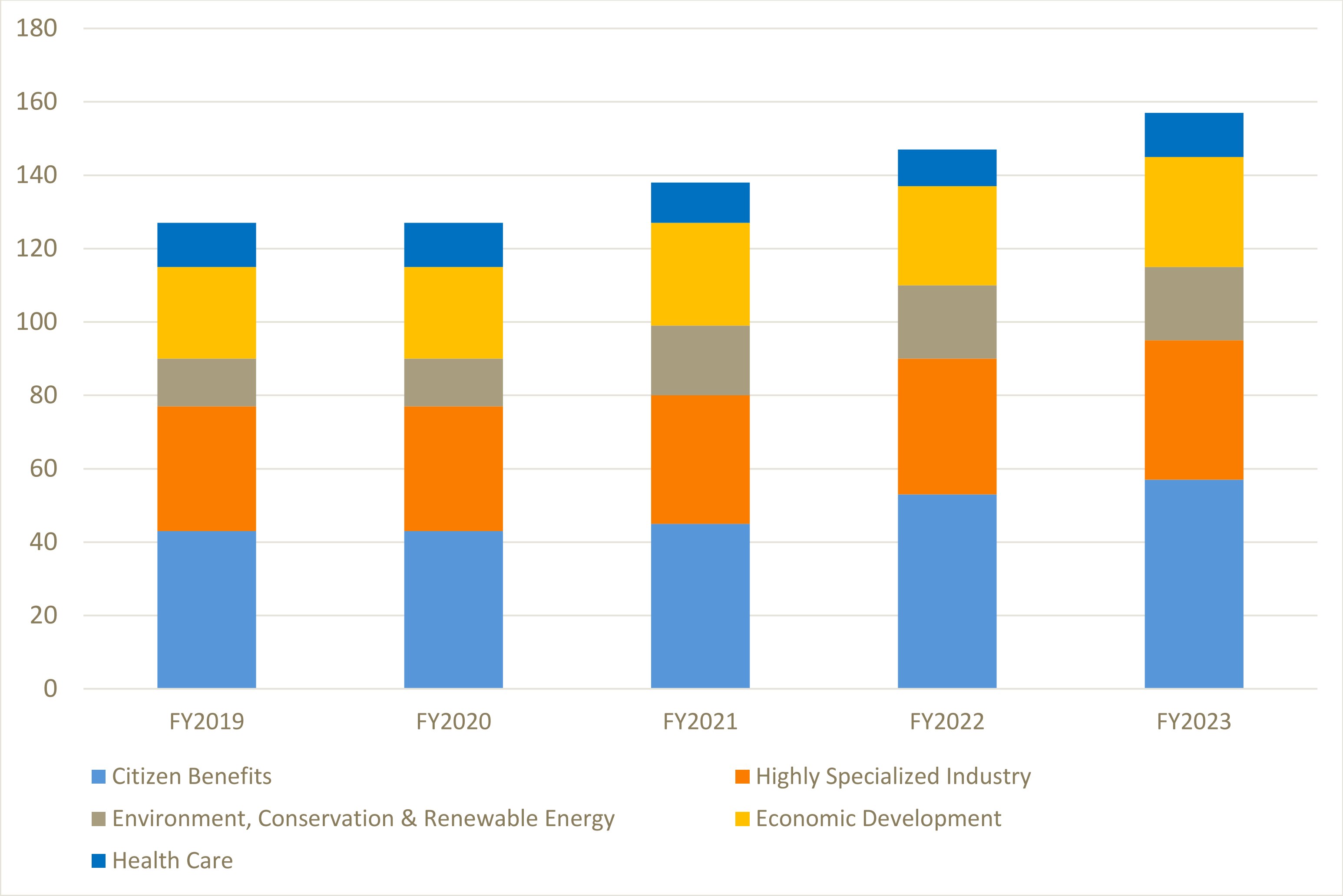
- Citizen Benefits: benefit all taxpayers or specific population (low-income, disabled, etc.), lessen the burden of taxation
- Economic Development: stimulate investment, job creation or job retention, attract industries
- Environment, Conservation, and Renewable Energy: support environmental health, promote conservation and renewable energy
- Health Care: increase access to or lower costs of health care
- Highly Specialized Industries: target specific or highly specialized industries

Tax Expenditures by Category ($ in thousands)



Number of Tax Expenditures by Category

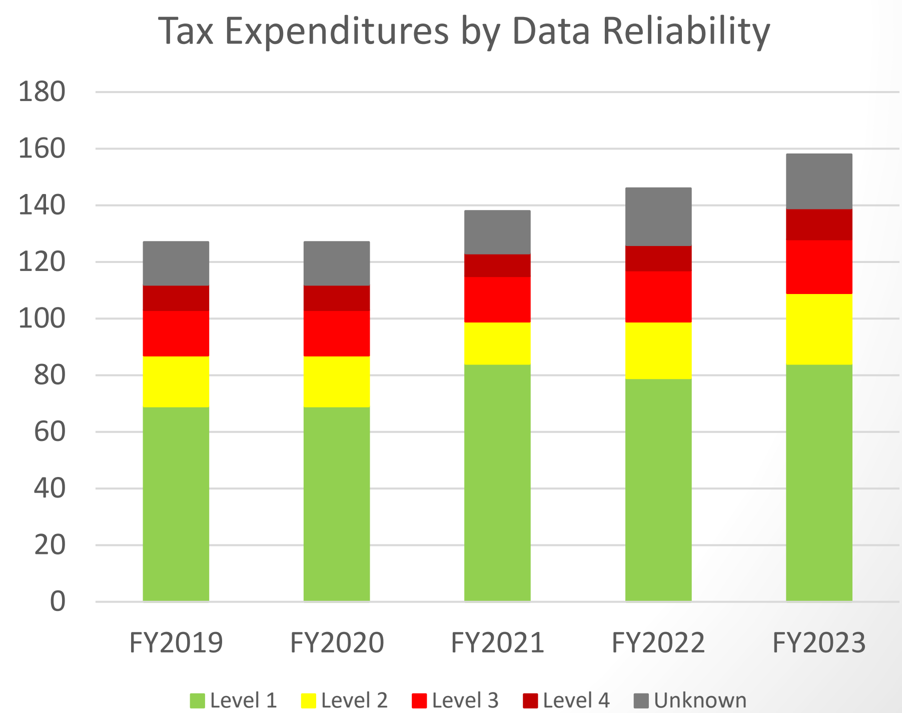
- 5 new citizen benefits tax expenditures–among 8 total new expenditures from 2022 and 2023 legislation
- 15 expired/obsolete tax expenditures were repealed effective July 1, 2023 (2023 SB147)



Expenditure Estimates – Data Reliability

- The estimated revenue foregone should be evaluated in conjunction with reliability factor
- Reliability depends on data available to Tax & Rev
  - Exemptions that are not reported will have low reliability
  - Deductions that are separately reported (28) will have higher reliability than deductions that are reported together
  - Credits have high reliability

Reliability Factor	Description
1	Most reliable. No estimation
2	Estimated from GenTax data
3	Estimated from national data
4	Least reliable. Estimated from limited data
Unknown	No data available



Expenditure Estimates – Data Reliability

- This year's report continues to have a special data reliability issue
- In July 2021, Tax & Rev upgraded to Version 12 of the Gentax system
- The upgrade included a more extensive drop down menu of GRT deduction codes in online filing system (TAP: Taxpayer Access Point)
- FY2022 & FY2023 data suggest taxpayers are mis-selecting GRT deduction codes
- Some GRT deductions are therefore likely overstated
- Tax & Rev has implemented a new drop down menu effective for FY2024 that directs taxpayers to select the appropriate GRT deduction codes
- Taxpayers are not paying the wrong tax amount, only selecting the wrong deduction code

	Fiscal Year	2021	2022	2023
Aircraft Sales or Services GRT Deduction	Taxpayers	0	56	50
	State General Fund Expenditure (thousands)	$0	$2,838	$1,666
	Local Government Expenditure (thousands)	$0	$1,892	$1,065

	Fiscal Year	2021	2022	2023
Durable Medical Equipment Deduction	Taxpayers	9	150	110
	State General Fund Expenditure (thousands)	$400	$5,800	$5,600
	Local Government Expenditure (thousands)	$200	$3,900	$3,600

New Additions in 2023 Report

Expenditures	Legislative Session	Category	2023 Amount ($000's) (Local and State)
Additional Income Tax Rebate 2021 Tax Year Filing	2023 Reg.	Citizen Benefits	694,320
Armed Forces Retirement Pay Exemption from PIT	2022 Reg.	Citizen Benefits	4,558
Certain Health Care Providers Federal Payments exemption from GRT – American Rescue Plan Act of 2021 (ARPA)	2023 Reg.	Health Care	4,700
Certain Health Care Providers Federal Payments exemption from GRT – Coronavirus Aid, Relief and Economic Security Act (CARES)	2020 1st Special	Health Care	1,200
Feminine Hygiene Products GRT Deduction	2022 Reg.	Citizen Benefits	152
Local Economic Development Act (LEDA) Special GRT Distributions	2021 Reg.	Economic Development	18,637
Nurses Credit Against PIT 2022 Tax Year Filing	2022 Reg.	Citizen Benefits	6,872
Sales of Services to Manufacturing GRT Deduction	2022 Reg.	Economic Development	1,144
Social Security Income Exemption from PIT	2022 Reg.	Citizen Benefits	71,480

New Additions in the 2023 Report – New Legislation & Reevaluations

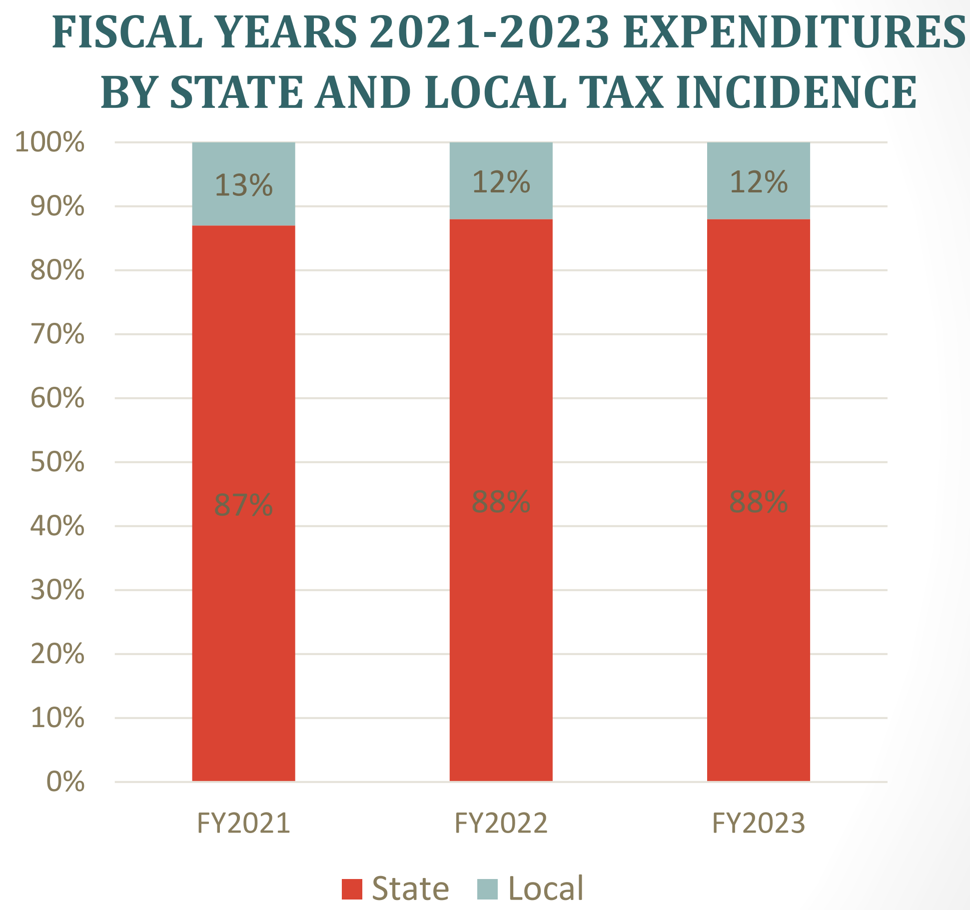
Not Tax Expenditures
Net Income subject to entity-level tax Exemption from PIT and CIT (7-2-5.12 and 7-2A-4.1 NMSA 1978)
Receipts of the Federal Government, State Government, Indian Nation, or Foreign Nation Exemption from GRT (7-9-13 NMSA 1978)
Sale of certain telecommunications services exemption from GRT (7-9-38-2 NMSA 1978)
Tax Paid to New Mexico Tribes Credit against Motor Vehicle Excise tax (7-14-7 (B) NMSA 1978)
Use of Property and Services by Federal, State or Local Governments Exemption from Compensating Tax (7-9-14A NMSA 1978)
Use of Property by Indian Nation, Tribe or Pueblo Exemption from Compensating Tax(7-9-14B NMSA 1978)
Tangible Personal Property Exemption from Property Tax (7-36-8 NMSA 1978)

Top Ten Expenditures by Cost: 2023 compared to 2022

Name	2022 ($000's State & Local)	2022 Rank	2023 ($000's State & Local)	2023 Rank	
Additional Income Tax Rebate 2021 Tax Year	0	NA	694,320	1	Green
Sale of Food at Retail Food Stores GRT Deduction and Hold Harmless Distribution	422,671	2	443,918	2	Green
Prescription Drugs, Oxygen and Medical Cannabis GRT and GGRT Deduction	371,700	3	392,500	3	Red
DOH-Licensed Hospitals 60 Percent GRT Deduction	201,975	5	196,111	4	Yellow
Capital Gain Deduction From PIT	102,483	8	114,533	5	Green
Film and Television Credit against PIT and CIT	60,532	12	100,240	6	Green
Working Families Tax Credit against PIT	104,527	7	93,802	7	Green
Health Care Practitioner Services GRT Deduction and Hold Harmless Distribution	76,672	10	76,588	8	Green
Social Security Income Exemption from PIT	0	NA	71,480	9	Yellow
Low-Income Comprehensive Tax Rebate, +65 and older additional rebate	62,265	11	60,363	10	Green

Tax Expenditure Incidence

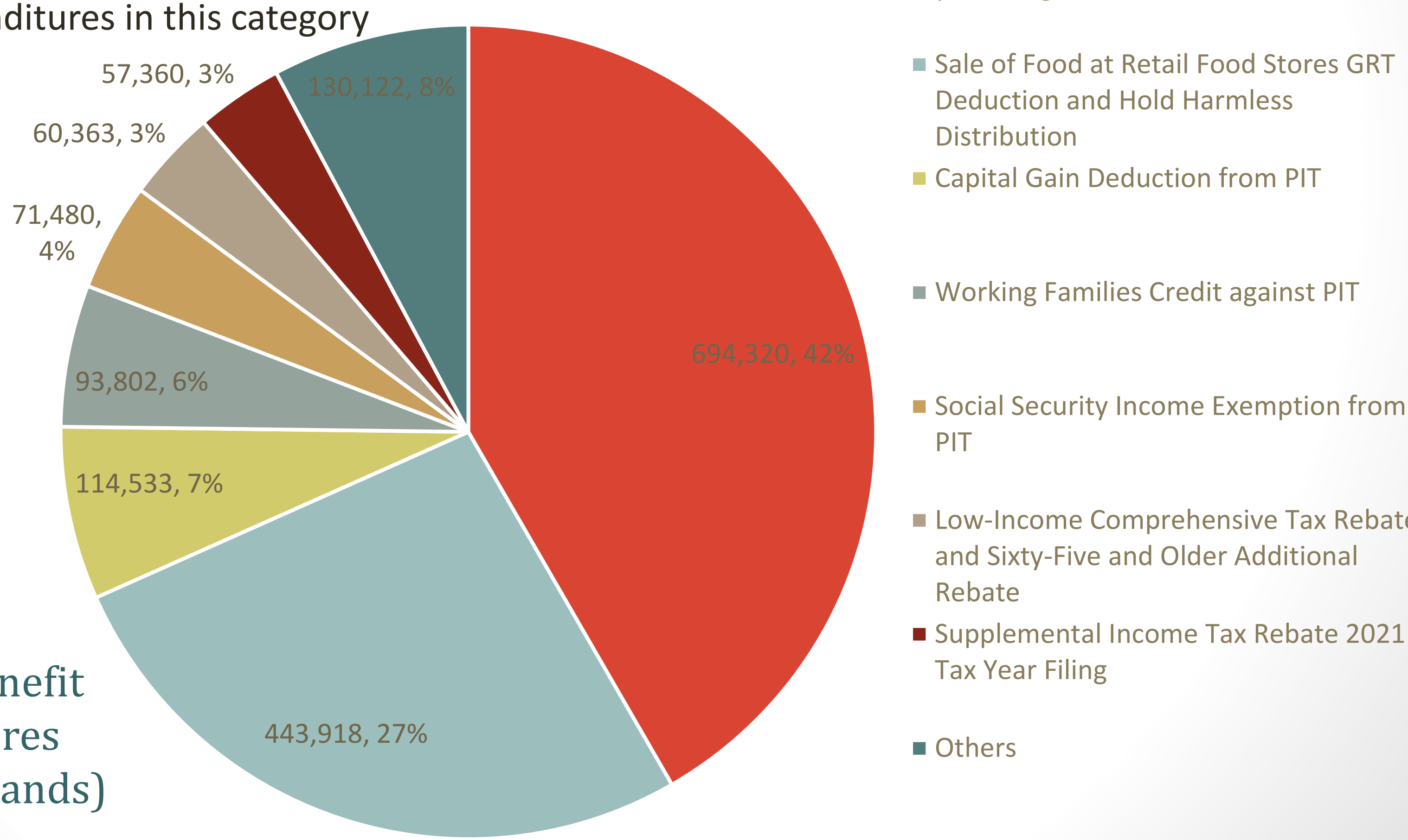
- GRT incidence for deductions and exemptions is shared between the State General Fund and local governments in most cases
- Tax expenditures for CIT, PIT, etc., generally impact only State General Fund directly
- Recent large rebates only impacted State General Fund



NOTE: DOES NOT INCLUDE PROPERTY TAX EXPENDITURES

Citizen Benefits

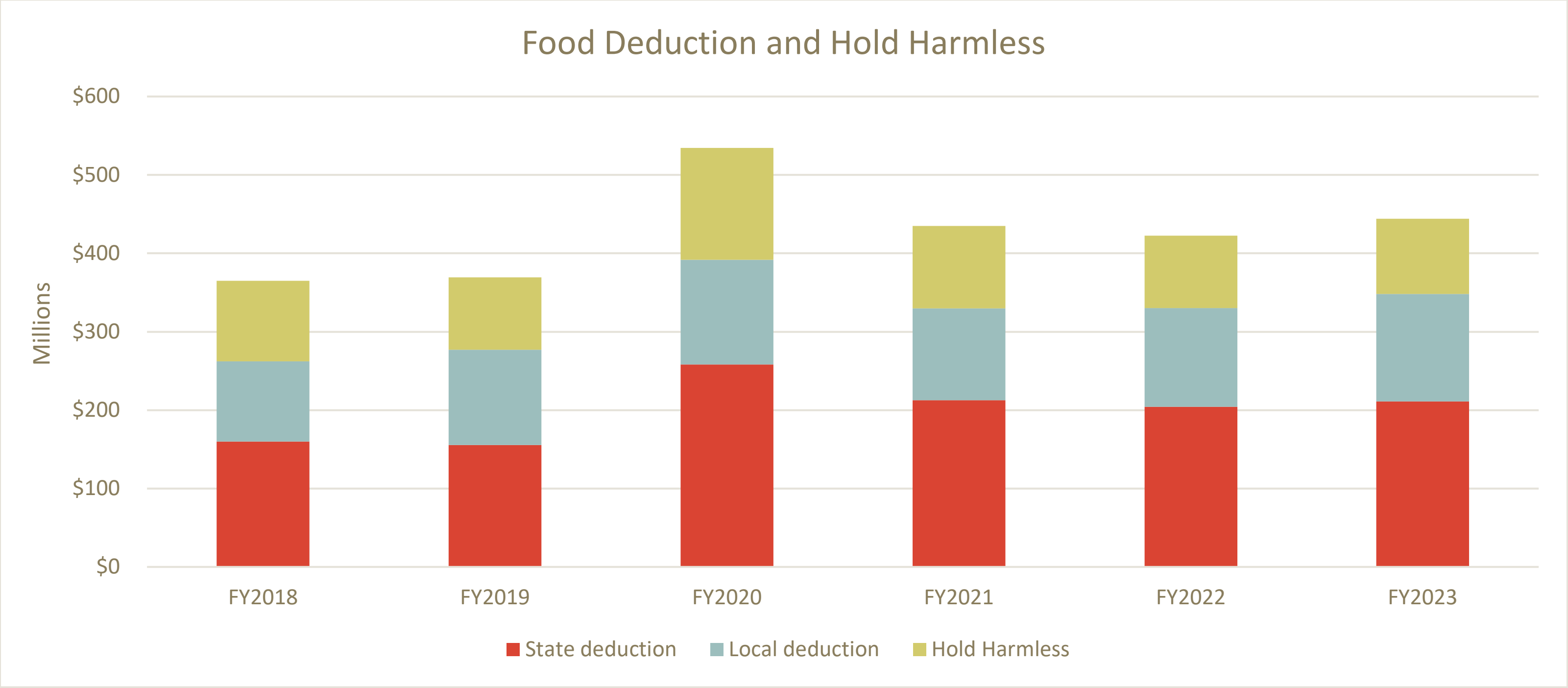
- Represent the largest share of tax expenditures in 2023 - $1.7 billion or 58%
- Large one-time 2021 tax year rebates increased this category significantly - $775.8 million total, with $694.3 million issued for the new rebate passed in the 2023 Legislative Session (HB547)
- Food deduction totaled $443.9 million up from $422.7 million in previous year
- New Expenditures: Social Security & Armed Forces Retirement Exemptions from PIT, Nurses Credit
- 58 Expenditures in this category



Citizen Benefit Expenditures (in $thousands)

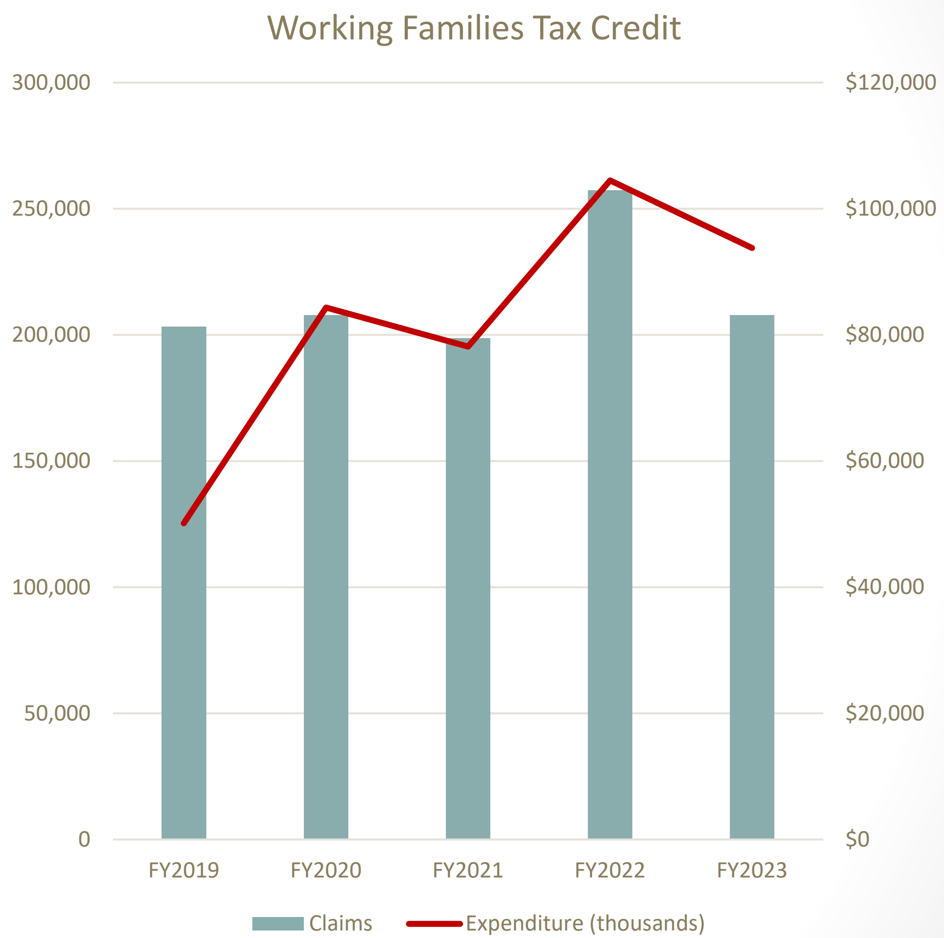
Citizen Benefits : Food GRT Deduction

- GRT deductions enacted in 2004 to reduce the cost of food and medical services
- Hold harmless provisions partially offset foregone local tax revenue as a result of the deductions
- 2013 legislation began a phase-out of the hold harmless payments to larger local governments scheduled to end in 2030
- 2022 amendment froze hold harmless phaseout for certain municipalities
- COVID-19 had striking impacts on the Food GRT Deductions in FY2020 as food consumption shifted away from restaurants and towards food purchased at grocery stores



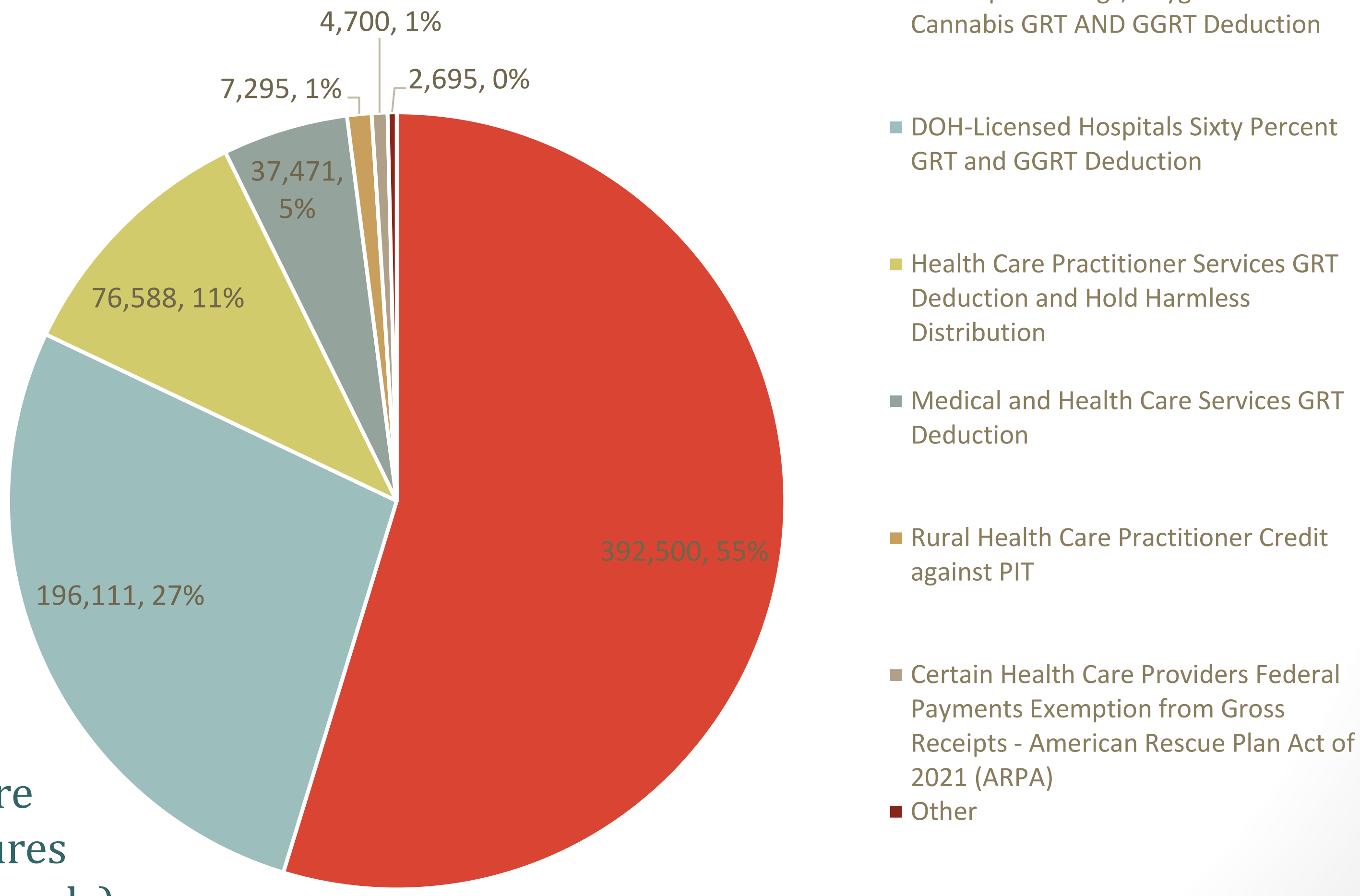
Citizen Benefits: Working Families Tax Credit

- Refundable PIT credit
- Enacted in 2007 at 8% of federal earned income tax credit (EITC)
- Increased to 10% EITC in 2008
- Increased to 17% EITC in 2019
- 2021 amendment:
  - increased to 20% EITC for tax years 2021 and 2022
  - Increased to 25% EITC tax years 2023 and on
  - Expanded eligibility to workers aged 18 to 25
  - Expanded eligibility to ITIN filers



Health Care

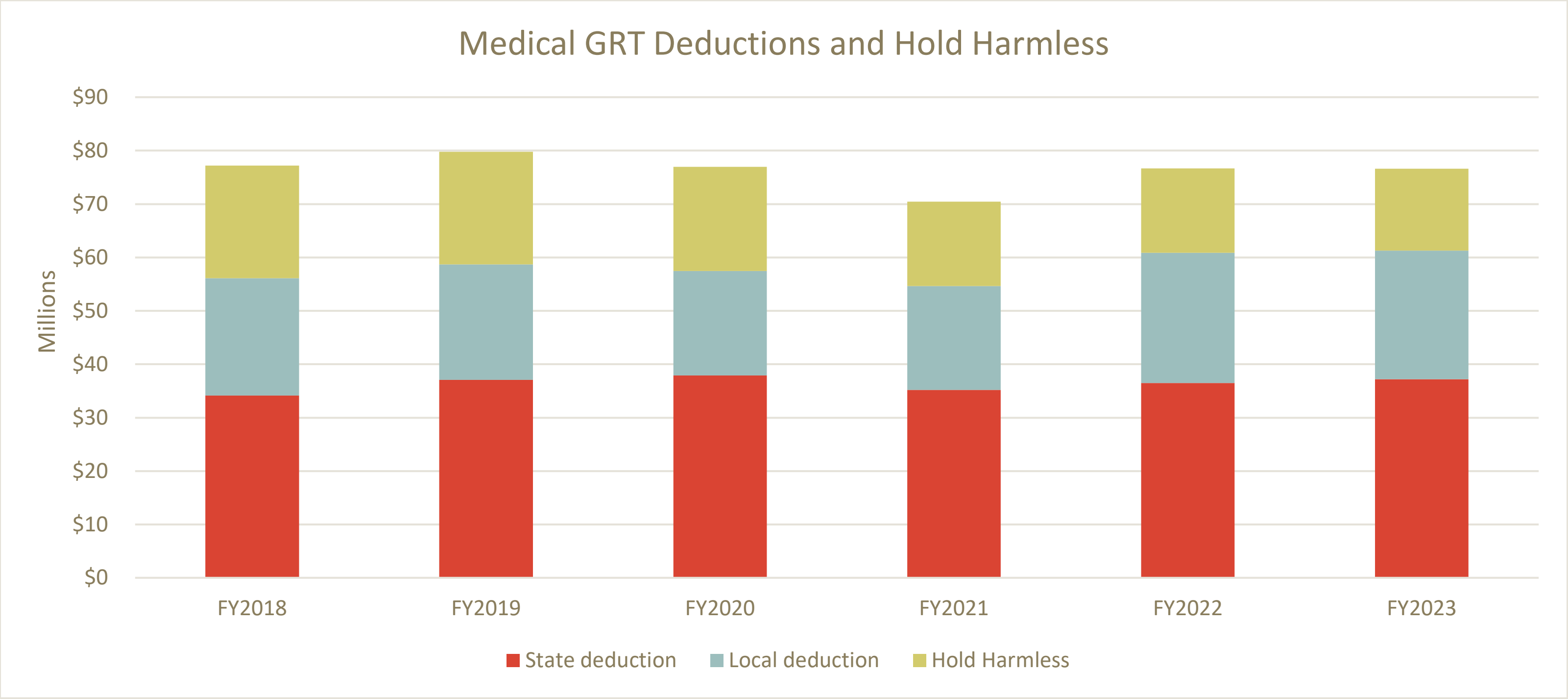
- Represents the second largest share of tax expenditures in FY23 - $717 million or 25%
- The largest reported contributor is the Prescription Drugs, Oxygen and Medical Cannabis GRT & GGRT Deduction at $393 million.
- 12 Expenditures in this category



Health Care Expenditures (in $thousands)

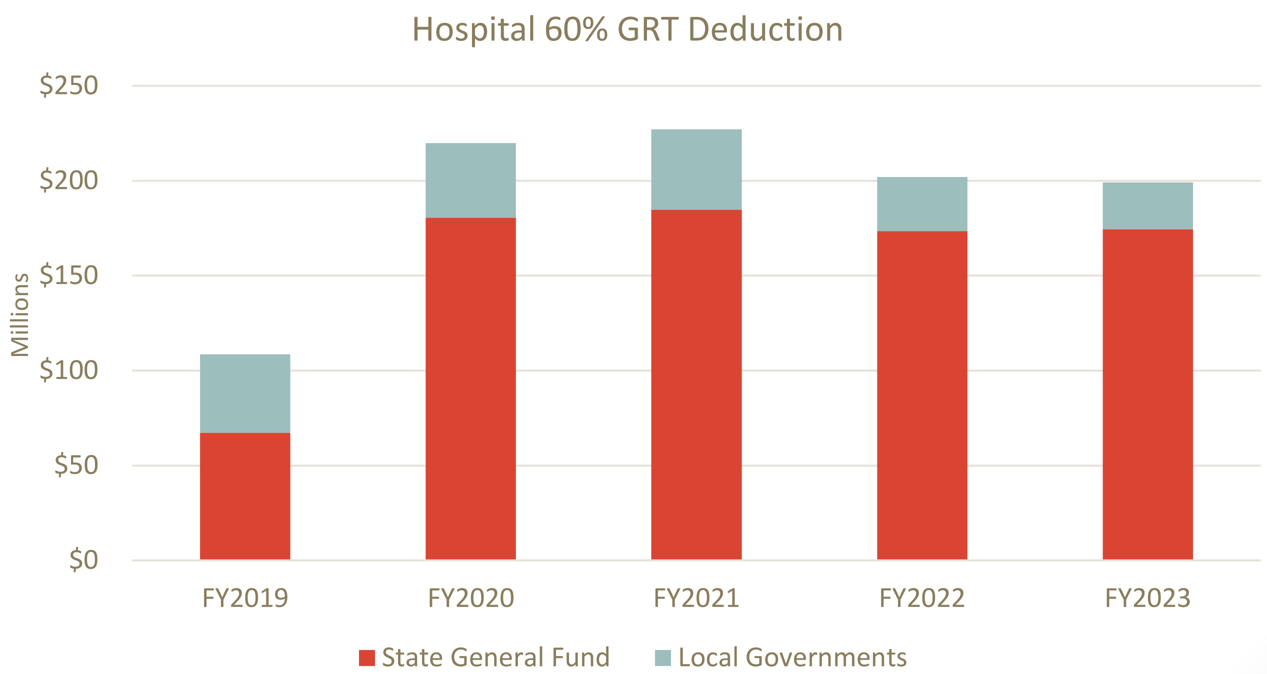
Health Care: Medical GRT Deductions

- GRT deductions enacted in 2004 to reduce the cost of food and medical services
- Hold harmless provisions partially offset foregone local tax revenue as a result of the deductions
- 2013 legislation began a phase-out of the hold harmless payments to larger local governments scheduled to end in 2030
- COVID-19 decreased medical deductions in FY20 and FY21 as individuals delayed medical care
- 2022 amendment froze hold harmless phaseout for certain municipalities
- 2023 amendment expands the deduction to include copays and deductibles



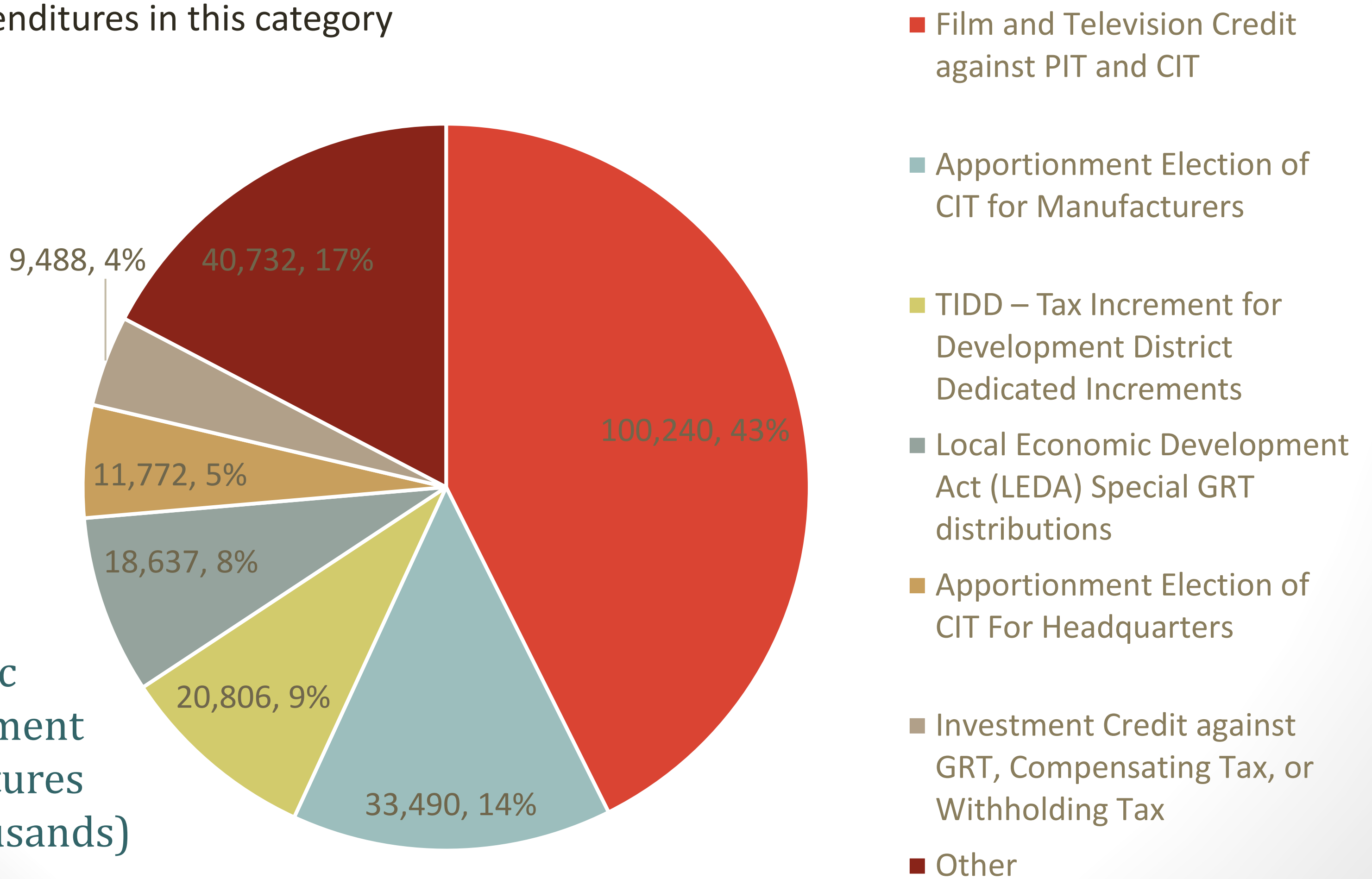
Health Care: Hospital GRT Deductions & Credits

- HB6 (2019) reformed hospital taxation to level the playing field between public, private and non-profit hospitals
  - Increased GRT deduction for private hospitals for medical services from 50% to 60%
  - Added non-profit and governmental hospitals into the tax base, allowing them the deduction
  - Non-profit and governmental hospitals are not subject to local government gross receipts taxes, so only the State General Fund deduction increased
  - Repealed a 5% credit to for-profit hospitals against their post-deduction gross receipts
- Hospital receipts rose in FY2020 and FY2021 due to COVID-19 hospitalizations



Economic Development

- Represents 8% of tax expenditures in FY23 - $235 million
- The largest reported contributor is the Film and Television Credit Against PIT and CIT at $100.2 million
- New Expenditure: LEDA Special GRT Distributions
- Moved TIDDs back as an expenditure from being classified as a non-expenditure last year
- 30 Expenditures in this category



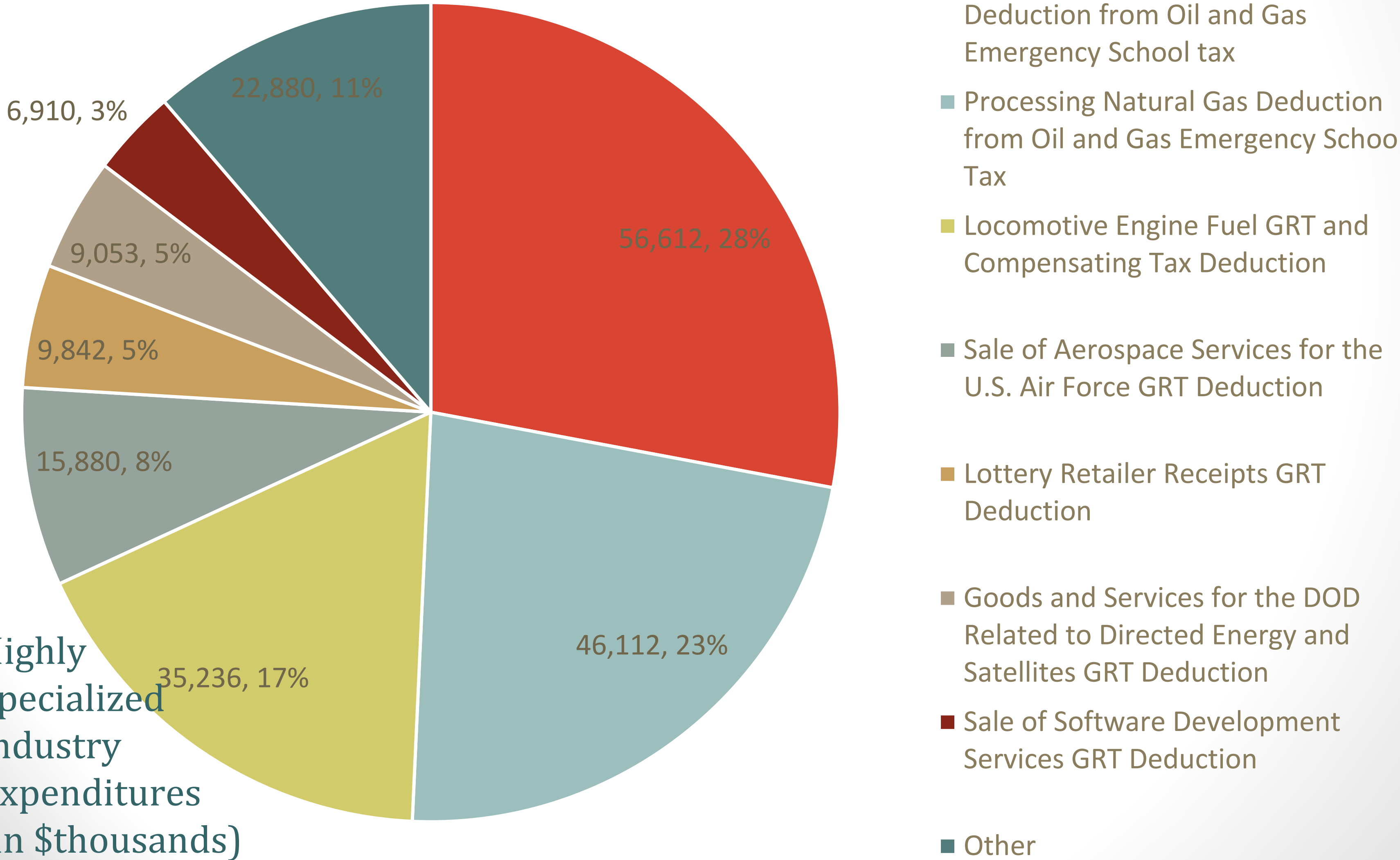
Economic Development Expenditures (in $thousands)

Economic Development: Film Tax Credit

- 2019 Legislation
  - Increased film credit cap from $50 million to $110 million
  - Created new category of film partners that are not subject to the cap
- FY19: $127 million in film credit backlog accrued under the previous $50 million cap was repaid in FY19 and FY20
- FY21: Film projects delayed as a result of COVID-19
- FY22 – FY23: Resumption of film projects and resulting credits
- 2023 Legislation
  - Increases the annual cap by $10 million for fiscal years 2024 through 2028, until a cap of $160 million

Highly Specialized Industry

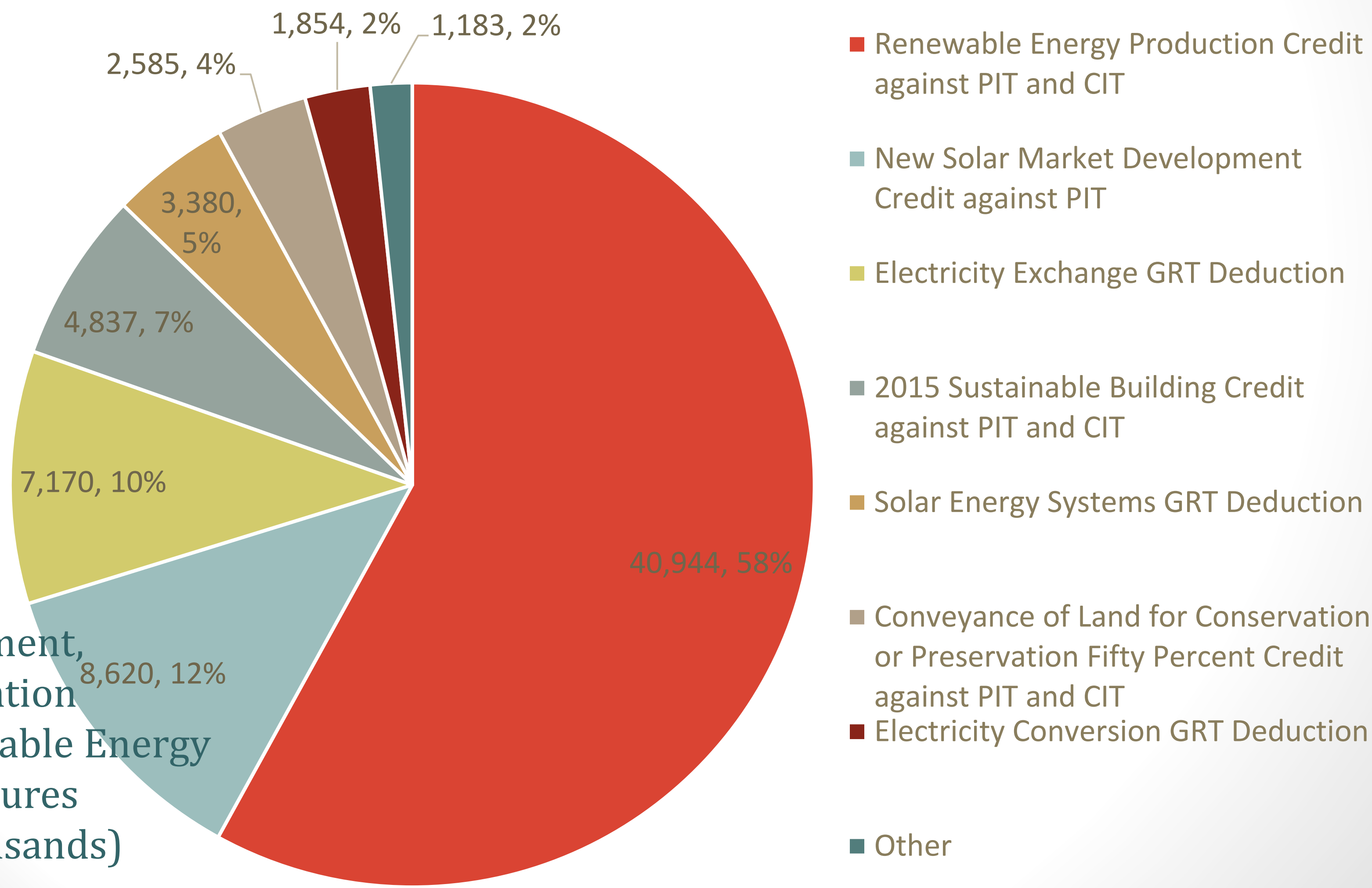
- Represent 7% of tax expenditures in FY23 or $203 million
- The largest reported contributor is the Transportation of Natural Gas Deduction from Oil and Gas Emergency School tax at $57 million
- 38 Expenditures in this category



Highly Specialized Industry Expenditures (in $thousands)

Environment, Conservation & Renewable Energy

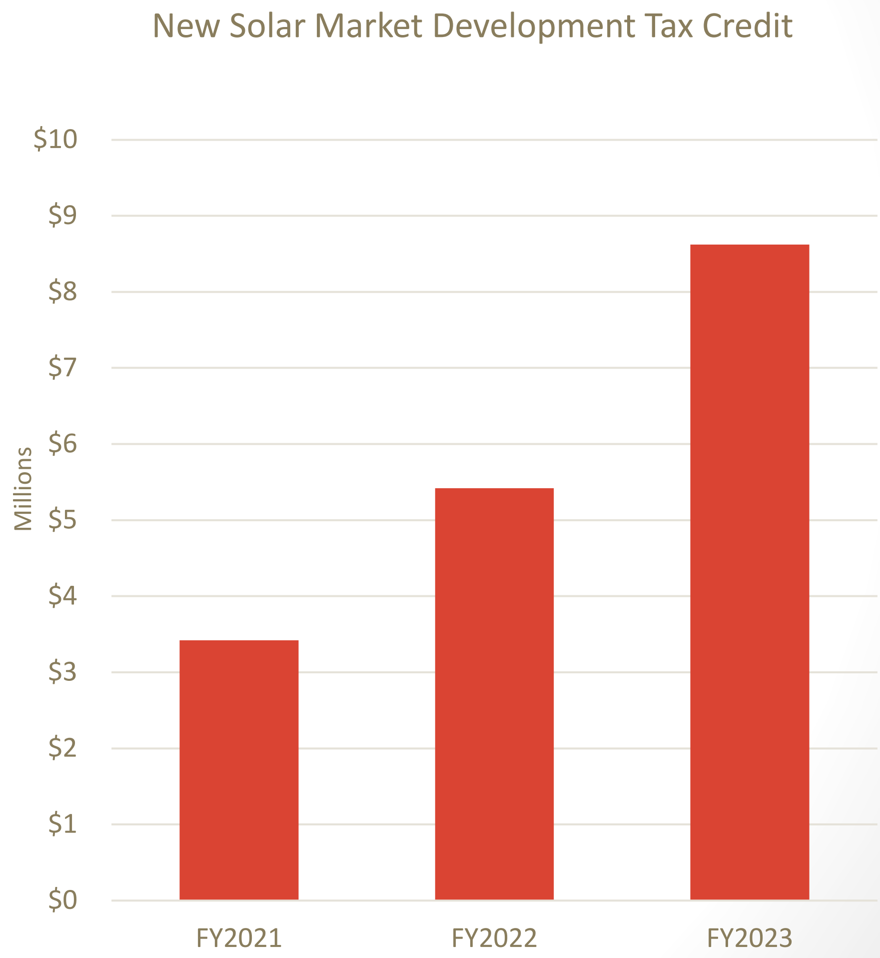
- Represent 2% of tax expenditures in FY23 or $71 million
- The largest reported contributor is the Renewable Energy Production Tax Credit against PIT and CIT at $41 million
- 20 Expenditures in this category



Environment, Conservation & Renewable Energy Expenditures (in $thousands)

Environment, Conservation & Renewable Energy: New Solar Market Development Credit

- New credit enacted in 2020, amended in 2022 to increase cap to $12 million
- Taxpayers who purchase and install a solar thermal system or photovoltaic system may apply for a $6,000 credit against PIT
- New credit can apply for full cost of purchase and installation versus 10% in original credit
- New credit is now refundable and transferable under 2022 amendments



Repealed Effective 7/1/2023

Name	Rationale for repeal	2023 ($000's)
Advanced Energy GRT and Compensating Tax Deduction	No claims to date. Construction of facility required prior to Dec. 31, 2015.	$0
Advanced Energy Credit Against GRT, Compensating Tax, Withholding Tax, PIT, or CIT	No claimants in Tax Year 2022. Fiscal impact in FY23 due to prior tax years. Construction of facility required prior to Dec. 31, 2015.	Redacted
Blended Biodiesel Fuel Credit against PIT and CIT	Credit has expired and carry-forward period ended in tax year 2017.	$0
Business Facility Rehabilitation Credit against PIT and CIT	No claims to date, there are no enterprise zones to establish eligibility.	$0
Electronic ID Reader Credit against PIT and CIT	Credit has never been claimed.	$0
Hybrid Vehicle Exemption from MVX	Exemption was effective until June 2009.	$0
Military Construction Services GRT Deduction	Sunset July 1, 2022	$0

Repealed Effective 7/1/2023

Name	Rationale for repeal	2022 ($000's)
Nonprofit Elderly Care Facility Exemption from GRT	Non-profit entities already qualify for GRT exemption based on status.	$990
Penalty Pursuant to Section 7-1-71.2 NMSA 1978 Credit Against GRT, Compensating Tax and Withholding Tax	Credit has not been available since July 1, 2010.	$0
Physician Participating in Cancer Treatment Clinical Trials Credit against PIT	Credit applied to tax years 2014-2016. The time period this credit could have been claimed has expired.	$0
Sales to Qualified Film Production Company GRT and GGRT Deduction	This deduction cannot be claimed by a film production company if they claim the film production tax credit.	Unknown
Vehicles Titled Before July 1, 1991 Exemption from Leased Vehicle GRT	At this point, this exemption applies to very few, if any, vehicles.	Unknown, but likely small
Venture Capital Investment Credit against PIT	No taxpayers have claimed this credit. It appears to compete with the net capital gain income deduction.	$0
Veteran Employment Credit against PIT and CIT	Credit applied to tax years 2012-2016 with carry forward of three years. Credit can no longer be claimed.	$0
Welfare-to-Work Credit against PIT and CIT	Tied to a federal program that no longer exists.	$0

Look Ahead – Expenditures with Sunsets next 5 years

Name	Note	Sunset Date	2023 ($000's)
Future Trust Distribution to a Nonresident Beneficiary Deduction from PIT (7-2-38 NMSA 1978)	Enacted 2019.	Jan. 1, 2025	$884
Unreimbursed or Uncompensated Medical Care Expenses Deduction From PIT (7-2-37 NMSA 1978)	Enacted 2015. Similar Credit and Exemption for Unreimbursed or Uncompensated Medical Care Expenses do not have sunsets.	Jan. 1, 2025	$5,459
Military Transformation Acquisition Program GRT Deduction (7-9-94 NMSA 1978)	Enacted 2005. Previously extended twice.	June 30, 2025	$968
Small Business Saturday Thanksgiving Weekend GRT Deduction (7-9-116 NMSA 1978)	Enacted 2018. Previously extended once.	July 1, 2025	$264
Angel Investment Credit against PIT (7-2-18.17 NMSA 1978)	Enacted 2007. Previously extended once.	Jan. 1, 2026	$1,135
Liquor License Lessor Deduction from PIT and CIT (7-2-40 & 7-2A-31 NMSA 1978)	Enacted 2021. Provides temporary relief to taxpayers affected by liquor license reform.	Jan. 1, 2026	$22
Liquor License Holders Deduction from GRT (7-9-119 NMSA 1978)	Enacted 2021. Provides temporary relief to taxpayers affected by liquor license reform.	July 1, 2026	$460

Look Ahead – Expenditures with Sunsets next 5 years

Name	Note	Sunset Date	2023 ($000's)
High-Wage Jobs Credit against Modified Combined Tax (7-9G-1 NMSA 1978)	Sunset is tied to definition of 'new high-wage' which must be created before July 1, 2026	July 1, 2026	$4,142
Armed Forces Retirement Pay Exemption from PIT (7-2-5.13 NMSA 1978)	Enacted 2022.	Jan. 1, 2027	$4,558
Technology Readiness Credit against GRT (7-9-96.3 NMSA 1978)	Enacted 2020. Previously extended once.	June 30, 2027	$1,040
Nonathletic Special Event at New Mexico State University GRT Deduction (7-9-104 NMSA 1978)	Enacted 2007. Previously extended three times	June 30, 2027	$128

Concluding Thoughts

- Legislative Thoughts
  - Purpose not always defined – difficulty to then evaluate
  - Sunset clause – forces evaluation of the expenditure where that is appropriate
  - Reporting requirements – electronic reporting: ease in working with other departments when cross-collaboration of expenditures; allows transparency; ability to evaluate expenditure cost
- Other Resources
  - National Conference of State Legislatures has a State Tax Incentive Evaluations Database (worked with Pew Charitable Trusts)
    - http://www.ncsl.org/research/fiscal-policy/state-tax-incentive-evaluations-database.aspx
  - Can compare different incentives across states, years, analysis, incentive type
  - U.S. Department of the Treasury, Federal Expenditure Reports
    - https://home.treasury.gov/policy-issues/tax-policy/tax-expenditures

Thank you!

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