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FISCAL IMPACT REPORT

SPONSOR Padilla/Campos **LAST UPDATED** _____
ORIGINAL DATE 2/16/2023
SHORT TITLE Wildfire Recovery Act **BILL NUMBER** Senate Bill 268
ANALYST Gray

REVENUE* (dollars in thousands)

Estimated Revenue			Recurring or Nonrecurring	Fund Affected
FY23	FY24	FY25		
	(\$4,410.0)	(\$4,410.0)	Nonrecurring	Personal Income Tax

Parentheses () indicate revenue decreases.

*Amounts reflect most recent analysis of this legislation.

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT* (dollars in thousands)

	FY23	FY24	FY25	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
Liability risk	Indeterminate but likely substantial				Recurring	General Fund
Tax change implementation	\$36.8	No fiscal impact	No fiscal impact	\$36.8	Nonrecurring	General Fund

Parentheses () indicate expenditure decreases.

*Amounts reflect most recent analysis of this legislation.

Sources of Information

LFC Files

Responses Received From

New Mexico Attorney General (NMAG)
 Taxation and Revenue Department (TRD)
 Environment, Minerals and Natural Resources Department (EMNRD)
 Office of the Natural Resources Trustee (ONRT)
 Public Schools Insurance Authority (PSIA)
 General Services Department (GSD)

No Response Received From

Public Regulation Commission (PRC)

SUMMARY

Synopsis of Senate Bill 268

Senate Bill 268 contemplates allowing people who suffered property damage or personal injury due to a wildfire to recover economic and noneconomic damages and attorney's fees. The bill creates definitions for who may be entitled to recovery, losses that are covered under the act, and the amounts that may be recovered. SB268 exempts these recoveries from state income tax.

Eligible losses. Under SB268, eligible losses include:

- Damage to real or personal property;
- Lost timber or other natural resources;
- Costs incurred during evacuation such as living expenses during displacement;
- Loss of use of damaged real or personal property;
- Loss of business and personal income;
- Other economic losses;
- Non-economic damages for emotional distress and personal injuries;
- Economic and non-economic damages for heirs of a person who is killed by a wildfire; and
- Attorney fees and expenses.

Tax exemption. SB268 contemplates exempting these recoveries from state income tax. Significant concerns were raised in agency analysis. As drafted, the bill is unclear whether it will exempt the provided recoveries from income tax as intended. New Mexico income tax is based off the federal income tax, and deductions must be written into the New Mexico tax code. SB268 does not amend the tax code and does not direct TRD to exempt or deduct damages from income. As written, the income tax provisions are not administrable. See fiscal implications and significant issues for further discussion.

Retroactivity. The bill provides that the recoveries are retroactively applicable to actions taken on or after January 1, 2022. Analysis from the Office of Attorney General (NMAG) flagged this provision as containing potential legal and constitutional issues, specifically as the retroactivity provision relates to federal law. See significant issues for further discussion.

Conflict with Federal and State law. Analysis from several agencies note that, as drafted, this bill may constitute the state's waiver of sovereign immunity under the New Mexico Tort Claims Act, which bars claims against state agencies. It is also unclear whether this bill conflicts with the Federal Tort Claims Act, which asserts the federal government's sovereign immunity.

SB268 is likely intended to address concerns raised regarding the scope of damages recoverable under the Hermit's Peak/Calf Canyon Fire Assistance Act, passed by Congress in 2022. However, language in the bill is vague and will likely not impact the compensation provided by the federal act. In fact, agency analysis notes that SB268 may result in the denial of federal reimbursements.

This bill does not contain an effective date and, as a result, would go into effect June 16, 2023, (90 days after the Legislature adjourns) if signed into law.

FISCAL IMPLICATIONS

Overview. SB268 intends to provide a tax exemption but, due to drafting issues, it is unclear whether it accomplishes its intention. New Mexico “piggy-backs” on federal income tax law for the definition of what is taxable income. When an individual files income tax in New Mexico, their income is determined based on their federal filing. Unless there is a specific deduction or credit, there is no mechanism to lower the taxable income. This bill does not amend the state’s tax code, and, as a result, is unclear how damages will be taxed or not. A person’s income will still be determined by federal tax law and the bill as currently written creates substantial ambiguity and is not administrable as written (see *Technical Issues*).

Analysis from the Taxation and Revenue Department (TRD) notes the bill “does not provide enough specificity to determine whether these types of funds are already exempt” or the scope of the exemption. TRD recommends specifying whether the income will be exempted or deducted from taxable income.

This analysis provides an estimate on the apparent *intent* of the bill, which is to exempt all recoveries from the state PIT. As noted above, the current language of the bill may not accomplish this, but the costs on page 1 provide the estimated revenue impact according to the apparent intent of the bill.

Clarity Issues Impact Estimates. The bill does not specify key factors that will determine the revenue impact, including:

- Against whom the injured persons may recover damages;
- Whether SB268 creates more opportunity for recoveries than current statute;
- How the commercial value of timber and natural resources should be calculated, what entity should calculate it, and what that value should be; and
- Whether the retroactive clause that makes actions taken after January 1, 2022 eligible for recoveries is constitutional.

A full list of issues with SB268 is outlined in significant issues, including several drafting issues that may impact the bill’s applicability and constitutionality.

Federal tax code. The Internal Revenue Service (IRS) defines the process for claiming disaster losses from federally defined major disasters, and disaster payments are generally considered tax exempt. As a result, SB268 may conflict with or duplicate federal tax law that already exempts recoveries from disasters from income tax.

Settlements or lawsuits are likewise governed by the Internal Revenue Code (IRC). IRC Section 104 provides an exclusion from taxable income with respect to lawsuits and settlements, but the circumstances under each settlement must be considered. According to the IRS website, the terms of a settlement are typically governing, and settlement parties are subject to information reporting requirements. If the settlement does not clarify whether awards are taxable, the IRS looks to the intent of the payor. If an award was made to replace lost income, those awards would be treated as income and be taxed. If made to replace property, physical injury, or wrongful death, they may be exempt.

SB268 contemplates exempting damages related to lost income, lost personal property, and other damages not specified by federal law. These changes are different from those provided by federal tax law, and specific deductions or credits would need to be provided for those to be exempted under the state PIT.

Estimate. It is assumed that it is the intent SB268 to exempt recoveries of wildfire damages. It is assumed there are \$200 million in cumulative damages related to the Hermit's Peak/Calf Canyon Fire eligible to be recovered in FY24 and FY25, and that 10 percent of those damages would already be tax exempt. The foregone revenue excluding that is estimated to be \$4.4 million in FY24 and \$4.4 million in FY25.

Estimate Method. To estimate the impact on PIT collections, this analysis first estimates the total annual damages due to wildfire. These are highly variable and no state agency tracks these in New Mexico. A 2010 study from the Western Forestry Leadership Coalition provides six case studies where property damage costs from wildfire range from \$400 thousand to \$864 million. The Hermit's Peak/Calf Canyon Fire damaged or destroyed about 900 homes for an estimated loss of \$180 million in property value.

Further, revenue impact estimates rely on the value of eligible losses. The bill defines a substantial list of eligible recoveries, including the "full commercial value" of lost timber or other natural resources. Under this condition alone, the total value of timber burned in the Hermit's Peak/Calf Canyon Fire could be over \$250 million.

Second, this analysis estimates the share of wildfire damages that would be recovered under current law, and the share of recoveries that are currently taxable. For this analysis, 10 percent of eligible damages are assumed to be currently taxable and are excluded.

Third, this analysis estimates how frequently this forgone tax revenue will occur. Major wildfires are infrequent. Just four wildfires burning over 1,000 square kilometers of land have occurred since 2000, but two of these occurred in 2022 (Hermit's Peak/Calf Canyon and Black Fire). Research indicates the risk of wildfires will continue to increase as anthropogenic climate change contributes to the aridification of the western U.S., including New Mexico. This analysis assumes a wildfire causing \$100 million in eligible damages will occur once every three years.

Lastly, this analysis estimates the applicable PIT rate to be 4.9 percent because over 80 percent of taxpayers are in the 4.9 percent income tax rate bracket.

Risk to the State. The General Services Department (GSD) maintains premium formulation for all risks waived under the New Mexico Tort Claims Act. According to GSD analysis, it is unclear how SB268 will interact with the Tort Claims Act. Currently, the state pays premiums for risks related to workers' compensation, general liability, law enforcement, medical malpractice, civil rights, automobiles, aircrafts, and blanket property. The total size of the risk pool across all agencies is about \$40 million.

If the state were to add litigation risks related to wildfires, the risk management costs could grow substantially. Wildfires often result in hundreds of millions of dollars in damages, an amount that would double or triple the current insurance pool. The liability risks associated with a wildfire started by a state employee during the execution of their duties is so significant that it may be uninsurable in the private market. The state would take on the full extent of the risk.

This analysis is unable to estimate the operating budget costs due to increased insurance risks, but it acknowledges they are likely to be significant.

Operating Budget Impact. TRD anticipates \$36.8 thousand in staff or contract costs to make annual information system changes and update forms, instructions, and publications.

SIGNIFICANT ISSUES

Overview. SB268 provides that eligible persons have a private right of action to recover wildfire damages. There are many significant issues with the bill as written. First, SB268 does not specify against whom the injured persons may recover damages. Second, the bill does not amend the tax code to provide either a deduction or an exemption. As a result, the bill as written may have limited or no impact on whether damages recovered are taxable. Third, analysis from several agencies raised legal and constitutional concerns related to the retroactivity provision. Fourth, conflict with federal laws may cause pending compensation to wildfire victims to be delayed, complicated, or denied. Lastly, due to the impact of climate change and the growing risks of wildfire in New Mexico, the bill may present significant liability risks for the state and other government entities.

Legal and constitutional concerns. SB268 is unclear regarding against whom a person may bring a civil action and from whom the person may recover damages. According to analysis from the Office of Attorney General (NMAG), if the bill intends to create a right of action against the federal government, it likely conflicts with the Federal Tort Claims Act. The federal government has sovereign immunity except as waived in the Federal Tort Claims Act.

Further, the state cannot authorize actions against the federal government or tribal governments and entities. The availability of relief for actions of such entities is controlled by the New Mexico Tort Claims Act, which seeks to balance the rights of the injured against the state. This bill contemplates disrupting that balance and may constitute a waiver of sovereign immunity by the state with regard to wildfires.

If the intent of the bill is to waive immunity for damages from wildfire, this may significantly increase the state's insurance risk. The state is required to insure all risks waived under the New Mexico Tort Claims Act. The growing risks of wildfire make this likely to be a significant cost.

Retroactive applicability provision. SB268 provides a retroactive effective date of January 1, 2022. According to the Cornell Law School Legal Information Institute's website, retroactive application of statutes are generally disfavored, a principle rooted in the Fifth Amendment of the U.S. Constitution (i.e., due process clause). In other words, "it is not considered fair for an individual to be liable for violating a law that did not exist at the time of the alleged violation."¹

Application of this analysis is further complicated because SB268 is likely intended to address the scope of damages recoverable under the Hermit's Peak/Calf Canyon Fire Assistance Act. But those damages are the result of actions by the federal government, and there are constitutional issues with applying statute retroactively to the federal government.

¹ See <https://www.law.cornell.edu/wex/retroactive>.

NMAG analysis addresses whether SB268 would be considered a retroactive provision, writing:

Although “[a] statute or rule is not retroactively construed when applied to a condition existing on its effective date even though the condition results from events which occurred prior to the date,” it will be considered retroactive “if it impairs vested rights acquired under prior law or requires new obligations, imposes new duties, or affixes new disabilities to past transactions.” *Howell v. Heim*, 1994-NMSC-103, ¶ 17, 118 N.M. 500

NMAG analysis also addresses the application of retroactive provisions. New Mexico and federal courts have held that retroactive application of substantive laws that create duties, rights, and obligations are disfavored. Further, SB268’s apparent intention to extend that retroactive application to the federal government may be unconstitutional. NMAG analysis writes:

The state can retroactively impose obligations on itself, but there may be constitutional limits on the state imposing new obligations on the federal government under an existing remedial federal law. “[T]he Legislature may pass a retroactive law operating on property belonging to the state, and such law will not be unconstitutional so long as private rights are not infringed.” *Pace v. Wight*, 1918-NMSC-081, ¶ 25, 25 N.M. 276.

The U.S. Supreme Court has held that a presumption against retroactivity should be applied and the statute made inapplicable “absent a clear indication from Congress that it intended such result.” *Fernandez-Vargas*, 548 U.S. at 38 (quoting *INS v. St. Cyr*, 533 U.S. 289, 316 (2001)).

However, even if legislation provides a clear indication that it intends retroactive application, there can still be due process concerns “if it impairs vested rights acquired under prior law or requires new obligations, imposes new duties, or affixes new disabilities to past transactions.” *Howell*, 1994-NMSC-103, ¶ 17.

NMAG analysis of the bill notes that because SB268 would retroactively impact existing rights and duties under the act, it raises those due process concerns.

Effect on the Hermit’s Peak/Calf Canyon Fire Assistance Act. SB268 is likely intended to address concerns raised regarding the scope of damages recoverable under the Hermit’s Peak/Calf Canyon Fire Assistance Act, passed by Congress in 2022. The act was passed to provide compensation for victims of the Hermit’s Peak fire, and it directs the Federal Emergency Management Agency (FEMA) to adopt regulations and establish a claims office with the purpose to compensate the victims of the fire for injuries sustained because of the fire.

NMAG analysis notes that it is unlikely SB268 would impact compensation authorized by Congress under the Hermit’s Peak/Calf Canyon Fire Assistance Act. The act specifies that “the laws of the State of New Mexico shall apply to the calculation of damages,” and the act therefore incorporated the laws of New Mexico as they existed at the time of the act’s passage. The state is unable to impose new requirements to federal law, even with SB268’s retroactivity provision.

The bill contains several conflicts with the federal act. As written, the bill contains a vague description of recoverable damages that appear to conflict with the federal Act. NMAG writes:

The Act’s explicit limitation on damages to only include “actual compensatory damages” would likely conflict with SB 268, Section 4, which includes undescribed “noneconomic” damages for individuals affected by the fire, regardless of whether they had any lost property.

NMAG analysis goes on to note that the act expressly limits recoveries to “actual compensatory damages measured by injuries suffered” and provides that damages shall not include “punitive damages.” The term “injury” within the act means an “injury or loss of property, or personal injury or death as used in [28 USCA §1346(b)(1)].” Section 103(5). The scope of what constitutes an injury is important since any claim against the federal government would need to be authorized and permitted by law in order to bypass any claim of sovereign immunity. SB268 conflicts with the actual damages requirement in the act because the bill would provide recovery for lost monthly rental value without requiring the previous use of the property as a rental.

Attorney fees. According to NMAG analysis, attorney’s fees are “collateral to the main cause of action” and are typically awarded based on the law in effect at the time of a decision. The Hermit’s Peak/Calf Canyon Fire Assistance Act does not appear to recognize attorney’s fees as part of actual compensatory damages. Yet, SB268 requires that attorney’s fees be awarded, likely in tension with the act.

Further, SB268 only requires that attorney fees be awarded and not the more common expenses like an appraiser, adjuster, accountant, or other expert required for a person to estimate the total value of their damaged and lost property. Further explanation of how damages are calculated may be explained by the FEMA regulations currently published in draft form but not yet finalized.

Distribution of recoveries. SB268 provides recoveries for wildfire damages but the bill provides no guidance on what entity will establish the recovery valuation or distribute those recoveries. Analysis from the Energy, Minerals and Natural Resources Department (EMNRD), notes that such a distribution and valuation program could conflict with or duplicate existing federal programs coordinated and implemented by the New Mexico Department of Homeland Security and Emergency Management.

EMNRD notes that the federal Hermits Peak Fire Assistance Act is currently in a rulemaking process to establish who and what can be funded via federal recovery funds. SB268, if enacted, may result in the denial of reimbursement under any or all of these programs or complicate their implementation.

Tax exemption. SB268 intends to provide a tax exemption but, due to drafting issues, it is unclear whether it accomplishes its intention. New Mexico “piggy-backs” on federal income tax law for the definition of what is taxable income. When an individual files income tax in New Mexico, their income is determined based on their federal filing. Unless there is a specific deduction or credit, there is no mechanism to lower the taxable income. This bill does not amend the state’s tax code, and, as a result, the impact on whether damages are taxable or not is unclear. A person’s income will still be determined by federal tax law, which, though it provides some exemption for recoveries received from settlements, likely does not go as far as SB268 intends.

The legislative drafting manual states that tax bills have a strong potential for litigation. Constitutional issues are “critical in tax legislation, including proper titles.” Notably, SB268 does not note in its title that it is relating to taxation and intends to amend the tax code.

Other. According to analysis EMNRD, the bill’s definition of wildfire may be problematic. As drafted, it is in direct tension with the commonly understood definition of wildfire which includes fires that are set intentionally, negligently, and naturally. SB268’s definition also

sweeps in all prescribed burns, agricultural burns, acequia burns, and cultural burns, regardless of context. The definition may even rationally extend to a house or business fire started as a result of arson or negligence.

SB268 does not clarify how a determination of the replacement value and full commercial value of timber will be made and which entity is responsible for this determination. Additional clarification of what constitutes timber and “other natural resources” is needed.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

SB268 is duplicative of existing statutes:

- Section 30-32-4, establishing “if any person shall set on fire any woods, marshes, prairies, whether his own or not, so as thereby to occasion any damage to any other person shall make satisfaction in double damages to the party injured, to be recovered by civil action.”
- Section 68-5-3, establishing a private landowner’s right to burn; and, in section 68-5-4, establishing liability associated with activities covered by the act.

TECHNICAL ISSUES

The bill provides damages not only for persons who had to flee a wildfire but also for persons who were killed by or suffered personal injury from a wildfire. As written, the bill could be read to exclude persons who did not flee and were killed or injured as a result, unless they also suffered a loss of property.

SB268 does not amend the tax code and does not direct TRD to exempt or deduct damages from income. As written, the income tax provisions are not administrable.

It is unclear whether SB268 constitutes a waiver of sovereign immunity. It appears to authorize a private citizen to bring civil action against the state, a mechanism reserved for the Tort Claims Act, Sections 41-4-1 NMSA 1978.

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