FISCAL IMPACT REPORT

		LAST UPDATED	
SPONSOR	Borrego/Sanchez	**ORIGINAL DATE**	2/25/25
SHORT TITLE	Home Fire Recovery Tax Credit	**BILL NUMBER**	House Bill 568
		ANALYST	Torres

REVENUE*
(dollars in thousands)

Type	FY25	FY26	FY27	FY28	FY29	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.
*Amounts reflect most recent analysis of this legislation.

Sources of Information

LFC Files

<u>Agency Analysis Received From</u>
New Mexico Attorney General (NMAG)
Taxation and Revenue Department (TRD)

SUMMARY

Synopsis of House Bill 568

House Bill 568 creates a second Home Fire Recovery Income Tax Credit, which provides an income tax credit for taxpayers who construct a new site-built home to replace a home destroyed by wildfire in calendar years 2021 through 2023. The credit applies only to taxpayers whose homes were destroyed by wildfire and who incur qualified site-built home expenditures for reconstruction on the same property. The credit is equal to the amount of qualifying expenditures with no caps or limits on credit amount, unlike the existing credit of $50,000 per home and $5 million per year. Furthermore, this credit expands the amount of the current credit by not requiring compensation from the state take place after other compensation and insurance. Any unused portion of the credit may be carried forward for up to three consecutive taxable years and is not refundable.

To claim the credit, a taxpayer must apply for certification of eligibility from the Construction Industries Division (CID) of the Regulation and Licensing Department within 12 months of completing the home. The application must include proof of property ownership, evidence of wildfire destruction, documentation of construction expenditures, and a sworn statement verifying the completion of the home. CID will issue tax credit certificates to eligible applicants and report these certifications to the Taxation and Revenue Department (TRD).

The credit is available for taxable years beginning on or after January 1, 2025, and the program will expire on January 1, 2032.

FISCAL IMPLICATIONS

A version of this credit already exists in current law (Section 7-2-18.35 NMSA 1978) as considered and amended in the 2024 tax package (HB252). This bill duplicates the credit by creating a new section of statute and repeating the credit rather than amending or repealing existing law. The costs represented in this analysis would be in addition to the costs of the existing credit for the same purpose. See Attachment 1 from the Taxation and Revenue Department highlighting the differences between the currently enacted credit from 2024 and the second credit proposed in this bill.

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. LFC research finds estimates of 430 homes 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 in the previous year, 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 and income tax credits could be highly variable and even under small to reasonable assumptions on construction could amount to \$420 million. The amounts and potential costs 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

[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

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 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

This bill was originally introduced in the 2024 legislative session and ultimately included in the tax package (HB252) and chaptered into law (7-2-18.35). It is unclear why the credit is being created as a new section of law, again, rather than amending the existing statute to accomplish the intent of the bill. This duplicates the credit already offered in Section 7-2-18.35 NMSA 1978, and creates confusion by having two credits of the same name. Unlike Section 7-2-18.35 NMSA 1978, this bill excludes manufactured homes, and only applies to homes with foundations, and that cannot be moved.

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.

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

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 would be supplanting federal dollars.

Construction Costs. Should the credit from this bill 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.

The New Mexico Attorney General adds:

> This bill may be subject to Anti-Donation Clause challenges. The Anti-Donation Clause provides, in pertinent part, that "[n]either the state nor any county, school district or municipality, except as otherwise provided in this constitution, shall directly or indirectly lend or pledge its credit or make any donation to or in aid of any person, association or public or private corporation[.]" N.M. Const. art. IX, § 14. A "donation," for purposes of Article IX, Section 14, is "a gift, an allocation or appropriation of something of value, without consideration." Vill. Of Deming v. Hosdreg Co., 1956-NMSC-111, ¶ 36, 62 N.M. 18. The Anti-Donation Clause is implicated in cases where, "by reason of its nature and the circumstances surrounding it," government funding or aid takes on the "character [of] a donation in substance and effect." Id. ¶ 37. Tax credits have been deemed to violate the Anti-Donation Clause. See, e.g., Chronis v. State ex rel. Rodriguez, 1983-NMSC-081, ¶ 30, 100 N.M. 342.
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> There are exceptions identified in N.M. Const. art IX, § 14, but they may not sufficiently address the tax credits in this bill. The exceptions are: (A) care and maintenance of sick and indigent persons; (B) & (G) veterans' scholarship programs for specified veterans; (C) loan programs for students of the healing arts; (D) new job opportunities in specified instances; (E)-(F) affordable housing; and (H) essential services, meaning infrastructure that allows for internet, energy, water, wastewater, or other similar services as provided by law. Although there may be instances in which a taxpayer seeking to take advantage of the tax credit identified in the bill satisfies certain of these exceptions—e.g., a recipient of a tax credit may be indigent or affordable housing may be implicated—the exceptions may not be broad enough to cover the intended tax credits as a whole.

TECHNICAL ISSUES

This bill creates a duplicate credit of an existing credit. Recommend amendments be made to the current Home Fire Recovery Tax Credit versus adding a duplicate credit. Taxpayers are currently applying for this credit on their 2024 tax return due April 15, 2025. This will add to the confusion if the current credit is duplicated.

The New Mexico Attorney General notes:

> HB568 in its current form does not cap reconstruction costs aside from the taxpayer's tax liability and the extent to which the credit could be carried forward for three consecutive taxable years.
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> It is unclear how Subsections (A), (C)(1)-(2), (H), and (J)(1)-(2) are intended to work together. As the bill is drafted, taxpayer homeowners who primarily resided in their home during the referenced wildfires are eligible for the credit. If a homeowner did not *primarily* reside in an impacted home because, for example, the home was the homeowner's second home, the home was rented out to someone else who primarily resided there, or the homeowner's children lived in the home, but the taxpayer homeowner still incurred expenditures for the construction of a site-built home on the same property as the prior wildfire-destroyed home, such taxpayer homeowner would nonetheless not be eligible for the credit.
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> Subsection (H), however, appears to provide credits to business entities and may reference the Corporate Income Tax Act. As written, Subsection (H) would allow for a taxpayer to be *allocated* the right to claim the credit from a *partnership or LLC* owned, at least in part, by the taxpayer. In order for this subsection to have any effect under the bill as otherwise drafted, it would need to be the case both that the taxpayer owns an interest in a partnership or LLC that owned a home destroyed by the referenced wildfires, and that the taxpayer lived in that home. This limited set of circumstances may have been intended, but the current iteration of the bill will likely raise questions regarding the applicability of the Corporate Income Tax Act.

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
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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 Principle	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	✘	
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	 ? ?	
Efficient: The tax expenditure is the most cost-effective way to achieve the desired results.	✗	
Key: ✓ Met ✗ Not Met ? Unclear		

IT/hj

Attachments:
1. Comparison of Credits

Attachment 1 – COMPARISON OF CREDITS

Detail	Existing Law (7-2-18.35 NMSA 1978)	Proposed New Bill (House Bill 568)
Effective Period	Effective until January 1, 2030	Effective until January 1, 2031
Tax Credit Amount	Up to $50,000 per home	Equal to the qualified site-built home expenditures
Aggregate Limit	$5 million per calendar year	No aggregate limit
Eligibility	Taxpayer who incurs expenditures for replacing a home that was destroyed by fire in calendar years 2021 through 2023	Taxpayer who incurs expenditures for replacing a home that was destroyed by fire in calendar years 2021 through 2023
Eligible Expenditures	Gross expenditures for construction or manufactured or modular home	Gross expenditures for the construction of site-built homes
Eligibility Application	Application to the construction industries division of RLD	Application to the construction industries division of RLD
Proof Required	Sworn statement, contract with builder/manufacturer	Sworn statement, contract with builder, site-built homes
Carry Forward Period	Can be carried forward for three consecutive years	Can be carried forward for three consecutive years
Joint Filers	Only one-half of the tax credit each	Only one-half of the tax credit each
Allocation to Business Entities	Proportional to ownership interest	Proportional to ownership interest
Annual Reporting	Annual report by Tax & Rev	Annual report by Tax & Rev
Home Definition	Includes site-built, manufactured, modular homes	Only site-built homes
Excluded Compensations	Excludes compensation from the Federal Hermit's Peak/Calf Canyon Fire Assistance Act, from insurance or other sources of compensation.	Excludes compensation from the Federal Hermit's Peak/Calf Canyon Fire Assistance Act