Fiscal impact reports (FIRs) are prepared by the Legislative Finance Committee (LFC) for standing finance committees of the Legislature. LFC does not assume responsibility for the accuracy of these reports if they are used for other purposes.

FISCAL IMPACT REPORT

		LAST UPDATED	
SPONSOR	Pope	**ORIGINAL DATE**	2/21/2025
SHORT TITLE	Certain Income Tax Exemptions	**BILL NUMBER**	Senate Bill 140
		ANALYST	Gray

REVENUE*
(dollars in thousands)

Type	FY25	FY26	FY27	FY28	FY29	Recurring or Nonrecurring	Fund Affected
PIT	**$0**	**($92,300)**	**($92,300)**	**($92,300)**	**($92,300)**	Recurring	General Fund

Parentheses ( ) indicate revenue decreases.
*Amounts reflect most recent analysis of this legislation.

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT*
(dollars in thousands)

Agency/Program	FY25	FY26	FY27	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
TRD	**$0**	**$14.6**	**$0**	**$14.6**	Nonrecurring	**General Fund**

Parentheses ( ) indicate expenditure decreases.
*Amounts reflect most recent analysis of this legislation.

Sources of Information

LFC Files

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

SUMMARY

Synopsis of Senate Bill 140

Senate Bill 140 (SB140) exempts all income tax for people with incomes up to $40 thousand for individuals and $60 thousand for taxpayers filing jointly. The bill does not contemplate any tax benefit for taxpayers earning more than the provided thresholds, creating a “cliff effect” where the two taxpayers who are otherwise identical pay significantly more. See *Significant Issues*.

This bill does not contain an effective date and, as a result, would go into effect 90 days after the Legislature adjourns if enacted, or June 20, 2025. The provisions of the bill are applicable to tax year 2025.

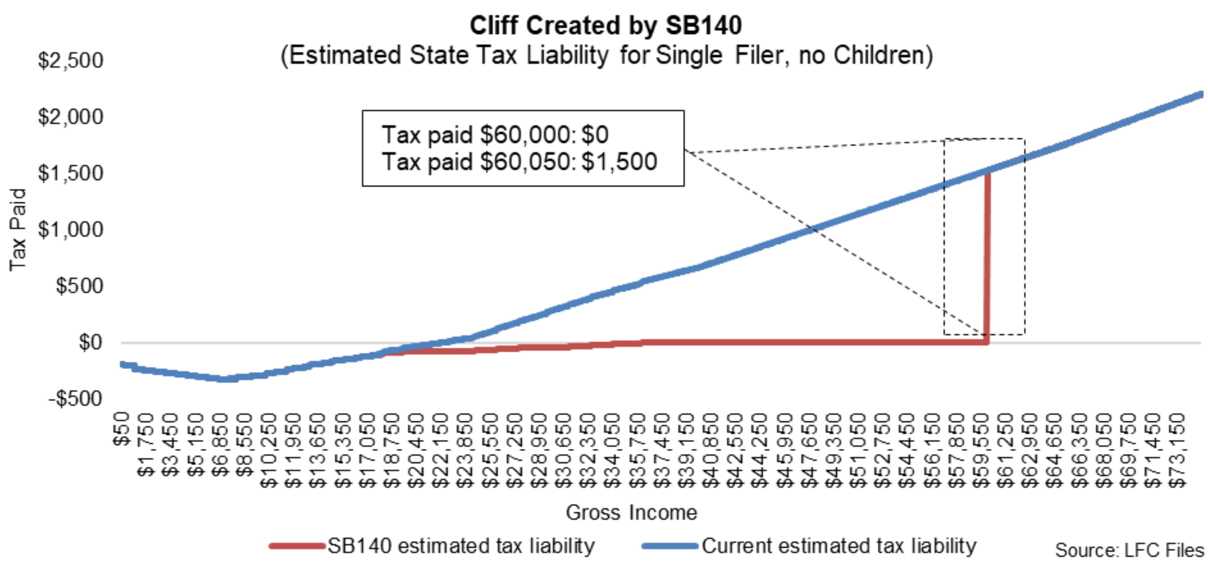
FISCAL IMPLICATIONS

This bill is expected to reduce recurring general fund revenue by $92.3 million beginning in FY26. The Taxation and Revenue Department (TRD) estimated the revenue impact using 2021-2023 tax return data for New Mexico individual taxpayers. The impact is modeled using the tax year 2025 brackets.

TRD estimates implementation of this bill will have a nonrecurring impact of $14.6 thousand on its IT expenses.

SIGNIFICANT ISSUES

SB140 creates a large income tax "cliff," where the amount a married taxpayer pays increases from $0 if they earn $60 thousand per year to $1,500 if they earn $1 more. Cliff effects are problematic for both equity and efficiency reasons because they penalize otherwise equal taxpayers and disincentives economic empowerment. This analysis uses a simulation of tax liability by income to discuss the impacts of the bill.



Consider a highway maintenance supervisor employed by the state who is the sole wage earner for their household. In December 2024, the worker received a $59 thousand annual salary. In January 2025, they receive a 2 percent out-of-cycle pay raise to recognize their experience and act as a retention incentive, bringing their salary up to $60,180 per year. Under SB140, instead of receiving a $1,180 raise, the state employee receives an effective pay cut of about $350, because of the dramatically increased tax liability they face once they cross the threshold of $60 thousand per year.

SB140 Scenario

Highway Maintenance Worker Supervisor:		Salary	Tax	Takehome
Pre-SB140	Before Raise	$59,000	$1,481	$57,519
	After Raise	$60,180	$1,530	$58,650
	Change	**+$1,180**	**+$49**	**+$1,131**
After SB140	Before Raise	$59,000	$0	$59,000
	After Raise	$60,180	$1,530	$58,650
	Change	**+$1,180**	**+$1,530**	**-$350**

TRD analysis similarly recognizes these cliff effects, pointing out that they "may also induce labor market disruptions as taxpayers may change their behavior to meet the exemption thresholds." While the above scenario is contrived, the cliff effects created by SB140 could have implications for tens of thousands of New Mexicans. Recent State Personnel Office data indicate that about 5 percent of state employees are one or two pay raises away from hitting the cliff effect created by SB140. Statewide, about 63 thousand taxpayers in total have income around this threshold, and over 350 thousand taxpayers could eventually be impacted by this cliff effect as wages rise due to inflation.

From a tax policy perspective, SB140 is inequitable. LFC Tax Policy Principles state that different taxpayers should be treated fairly, recognizing their individual ability to pay. Under this proposal, a person earning $20 thousand has the same tax liability as a person earning $40 thousand, even though that person has twice the ability to pay income taxes.

TRD analysis notes that policymakers may wish to consider how the exemption provided by SB140 will interact with other exemptions already provided by law. For example, the low- and middle-income exemption provides a partial exemption for taxpayers with incomes below $27.5 thousand for single filers and $55 thousand for married filers. TRD notes that SB140 may negate this exemption and "recommends that the tax code be adjusted to account for different interactions among exemptions, deductions and credits if this bill is enacted."

TECHNICAL ISSUES

TRD notes several technical issues:

> The filing status of "Heads of Household" or "Surviving Spouses" is omitted from this bill. TRD suggests adding ", heads of household and surviving spouses" after "returns" on line 25. So that it reads "C. married individuals filing joint returns, heads of household and surviving spouses with . . ."
>
> New Mexico uses adjusted gross income for the starting point to calculate state taxable income. This bill exempts income based on modified gross income (MGI), which adds a layer of complication for exempting income. MGI is used mostly for determining eligibility under 7-2-14 NMSA 1978, low-income comprehensive tax rebates. MGI includes income that may already not be taxable, like public assistance, alimony payments, railroad retirement, social security, etc. (see definition below). MGI should be reconsidered as the type of income that is exempt, this might be better replaced with "federal adjusted gross income" (FAGI). Most states use FAGI for the starting point of returns.
>
> "Modified gross income" (7-2-2 L. NMSA 1978) means all income of the taxpayer and, if any, the taxpayer's spouse and dependents, undiminished by losses and from whatever source, including: compensation; net profit from business; gains from dealings in property; interest; net rents; royalties; dividends; alimony and separate maintenance payments; annuities; income from life insurance and endowment contracts; pensions; discharge of indebtedness; distributive share of partnership income; income in respect of a decedent; income from an interest in an estate or a trust; social security benefits; unemployment compensation benefits; workers' compensation benefits; public assistance and welfare benefits; cost-of-living allowances; and gifts.

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

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.	×	This proposal was not vetted by an interim tax committee.
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	 × × ×	This bill does not have these components.
Transparent: The tax expenditure requires at least annual reporting by the recipients, the Taxation and Revenue Department, and other relevant agencies	?	The expenditure will likely be included in TRD's tax expenditure report, although that is not clear in the bill.
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	 × ×	The bill does not contain an 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	 ? ?	It is unclear whether this proposal is the most effective and efficient because measurable goals are not established.
Efficient: The tax expenditure is the most cost-effective way to achieve the desired results.	×	
Key: ✓ Met × Not Met ? Unclear		

BG/rl