FISCAL IMPACT REPORT

		LAST UPDATED	2/12/2025
SPONSOR	Lente/Martinez	**ORIGINAL DATE**	2/11/2025
SHORT TITLE	Earned Income Tax Credit	**BILL NUMBER**	House Bill 14
		ANALYST	Gray

REVENUE*
(dollars in thousands)

Type	FY25	FY26	FY27	FY28	FY29	Recurring or Nonrecurring	Fund Affected
PIT	$0	($73,300.0)	($74,900.0)	($76,600.0)	($78,300.0)	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 14

House Bill 14 (HB14) replaces the working families tax credit (WFTC) with the New Mexico earned income tax credit (EITC). There are two features to the expansion:

- First, it increases the amount of tax credit accumulated for each dollar a taxpayer earns. This means that every taxpayer currently receiving the WFTC will receive more under this proposal.
- Second, it increases income eligibility for all taxpayers, with the largest increase made for low-income adults without minor children.

Currently, the WFTC offers a 25 percent match of the federal EITC. EITC is a refundable tax credit that boosts the income of eligible low-income workers, especially those with children. Because the credit is refundable, an EITC recipient need not owe income taxes to receive the benefit. The EITC depends on a recipient's earned income. Specifically, the EITC phases in as a percentage of earned income (the "credit rate") until the credit amount reaches its maximum level. The EITC then remains at its maximum level over a subsequent range of earned income, between the "earned income amount" and the "phaseout amount threshold." Finally, the credit gradually decreases to zero at a fixed rate (the "phaseout rate") for each additional dollar of adjusted gross income (AGI) (or earned income, whichever is greater) above the phaseout amount threshold.

HB14 partially decouples New Mexico from the federal EITC. The definition of earned income remains the same as current law, but the bill defines a new credit rate, earned income amount, phaseout amount threshold, and phaseout rate. Under this bill, the effective New Mexico credit is equal to 30 percent of the federal EITC, meaning a taxpayer will get an at least 20 percent larger credit for each dollar of earned income compared to WFTC (i.e., 25 percent in current law increased to 30 percent by HB14).

Eligibility is expanded significantly for taxpayers without children, increasing from about $17 thousand per year to $35 thousand per year. Income eligibility is increased as follows:

Proposed Income Eligibility Limits, Current WFTC & EITC vs HB14 Proposed

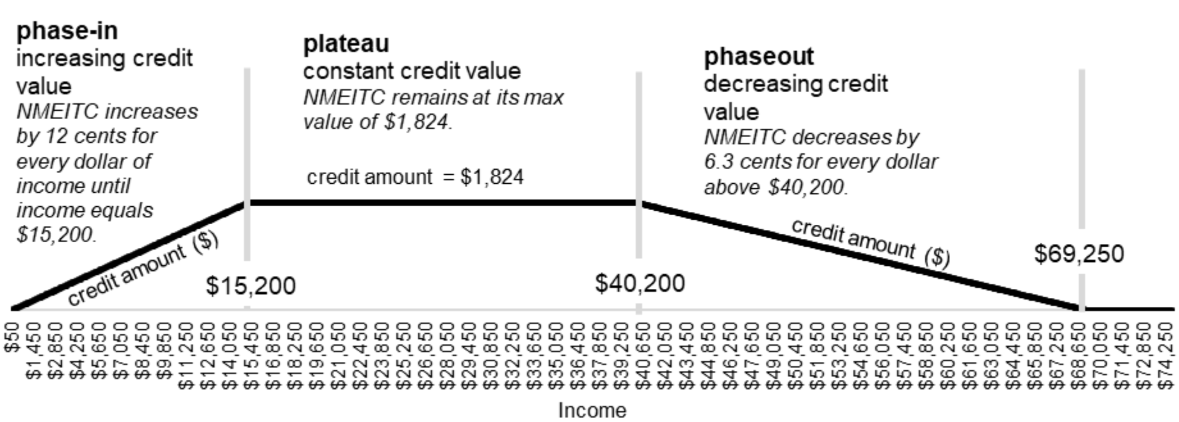
	WFTC & EITC	Proposed
No children, unmarried	$17,640	$35,300
1 child, unmarried	$46,560	$54,450
2 children, unmarried	$52,918	$64,250
3 or more children, unmarried	$56,838	$67,850
No children, married	$24,210	$40,300
1 child, married	$53,120	$59,450
2 children, married	$59,478	$69,250
3 or more children, married	$63,398	$72,850

The estimated benefits by taxpayer income and the number of dependent children is reflected below.

Maximum Benefits by Number of Children

No children, less than $35,000	$184
1 child, less than $54,000	$1,122
2 children, less than $64,000	$1,824
3 or more children, less than $67,000	$2,052

Example NM EITC for a Married Taxpayer with Two Children, by Income



Note every taxpayer getting WFTC will get more benefit under this expansion.

Source: LFC Analysis of HB14

Additional Changes. Taxpayers between 18 and 25 years old remain eligible as they are currently under WFTC. The bill creates a minimum credit amount for taxpayers earning less than $25 thousand per year equal to $100. All provisions of the credit are indexed to inflation. Lastly, section G requires the Taxation and Revenue Department (TRD) to reflect the value of the credit in tables with income brackets of $50, the same method required by the federal EITC.

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

FISCAL IMPLICATIONS

This bill is estimated to reduce recurring general fund revenues by $73 million in FY26, with the total cost growing to $78 million by FY29. LFC staff estimated this impact by simulating the value of the credit for and number of all taxpayers by income. The cost of the expansion was grown by consumer prices forecast from S&P Global.

In general, there are three categories of increased cost. The first group, taxpayers who are currently eligible for the credit but who do not benefit from the extended eligibility criteria, will see their credit increase by 20 percent per dollar earned, and the state will see a proportional increase in costs. The second group, taxpayers who are still eligible for the credit and whose incomes are sufficiently high to benefit from extended eligibility, will see their credit increase by a range of 21 percent per dollar earned to well over 200 percent per dollar earned because the value of the WFTC approaches zero in this range. The last group is taxpayers who are not currently eligible. This analysis estimates there are at least 75 thousand New Mexico who do not currently qualify for the WFTC who would under this proposal and would receive a benefit ranging from $184 to $2,052, depending on the number of dependent children.

The Taxation and Revenue Department (TRD) estimates that the bill will reduce recurring general fund revenues by $42.7 million in FY26. TRD analysis did not simulate the credit but estimated the marginal credit increase by taxpayer type. The agency assumes there are two types of taxpayer. First, there are those who currently receive the WFTC. The agency assumes costs to this group increase by 20 percent. Second, there are those who do not currently receive the WFTC. The agency assumes costs to this group by the value of the credit. The agency estimates there are 101.9 thousand New Mexico taxpayers who would be newly eligible for the expanded EITC under HB14.

LFC notes that TRD does not include a cost estimate for those who currently receive the credit but will receive an increase greater than 20 percent due to the changed eligibility criteria. Accordingly, this analysis uses the higher of the two estimates. This could be changed with the availability of new data.

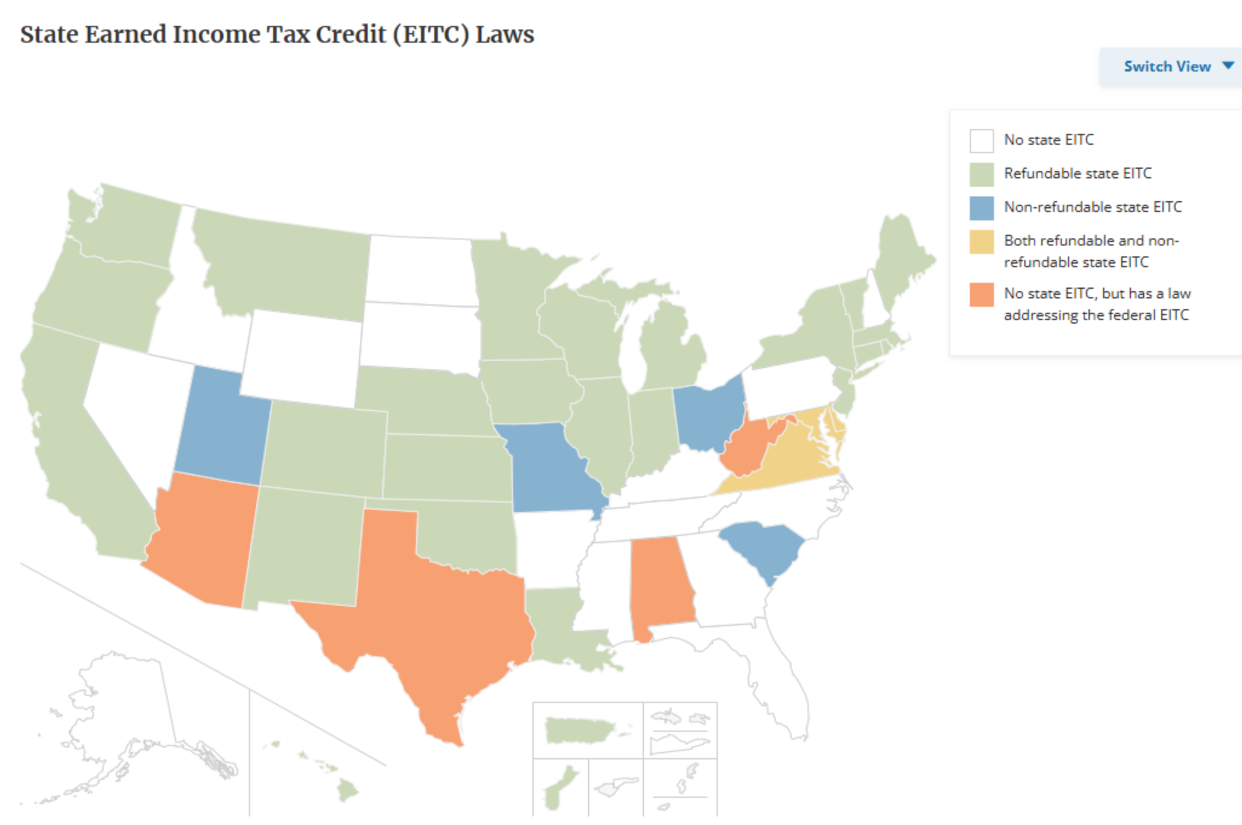
This bill creates or expands a tax expenditure. Estimating the cost of tax expenditures is difficult. Confidentiality requirements surrounding certain taxpayer information create uncertainty, and analysts must frequently interpret third-party data sources. The statutory criteria for a tax expenditure may be ambiguous, further complicating the initial cost estimate of the fiscal impact. Once a tax expenditure has been approved, information constraints continue to create challenges in tracking the real costs (and benefits) of tax expenditures.

Operating budget. TRD estimates the provisions of the bill will increase nonrecurring costs to the agency by $53.8 thousand in FY26 and by less than $1,000 on a recurring basis. The $400 recurring cost is omitted from the table on page 1.

SIGNIFICANT ISSUES

A 2024 LFC program evaluation titled *Improving New Mexico's Workforce Participation* recommended the Legislature increase the WFTC to "target noncustodial parents and childless workers to soften the benefits cliff and facilitate the reemployment transition for at-risk New Mexicans." This legislation accomplishes that recommendation by raising the benefit for workers without minor children and nearly doubling the eligibility threshold.

According to the National Conference of State Legislatures, 27 states have a refundable earned income tax credit. Most states tie it directly to the federal EITC, but several states have decoupled from the federal EITC as is contemplated by HB14.



Source: NCSL

The federal EITC is one of the largest anti-poverty programs in the United States. Researchers have documented how the federal EITC affects labor supply by creating a significant work incentive. For example, the introduction and expansion of state EITCs has been associated with an increased likelihood that a family with below-poverty level earnings in one year have earnings above the poverty threshold in the next year. Literature has associated federal EITC with improved outcomes for children's education, infant and child health, and parental health.

TRD analysis points out that that EITC is an incentive that can provide tax relief to families to help "offset the costs of raising children and can effectively reduce poverty rates." The agency writes that, although New Mexico has the highest official poverty rate in the nation for those under 18, supplemental measures at the federal and state level reduced poverty in New Mexico dramatically. The supplemental poverty rate for those under 18, taking into account the federal child tax credit, and is 8.9 percent. This is compared to New Mexico's official poverty rate of 27.4 percent. No other state saw as dramatic a reduction between the two measures for the period 2021 through 2023.

TRD analysis notes that the bill increases the administrative complexity for both the agency and for taxpayers. The agency writes of the increased tax code complexity:

> This complexity can create confusion for taxpayers, as they will need to accurately determine their eligible credit percentage and phaseout amount based on their specific circumstances when they file their New Mexico personal income tax returns. While the state will provide tables for taxpayers to estimate their credit, taxpayers will be estimating two different credits at the federal and state level.

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?
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	

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