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	Gonzales/Sanchez/Mejia/Vincent/Herrera	**ORIGINAL DATE**	2/14/2025
SHORT TITLE	Small Business Disaster Relief Tax Credit	**BILL NUMBER**	House Bill 326
		ANALYST	Gray

REVENUE*
(dollars in thousands)

Type	FY25	FY26	FY27	FY28	FY29	Recurring or Nonrecurring	Fund Affected
PIT	$0	($19,000)	($19,000)	($19,000)	($19,000)	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
EDD	$0	$416.7	$416.7	$833.4	Recurring	General Fund

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

Sources of Information

LFC Files

Agency Analysis Received From
Economic Development Department (EDD)
New Mexico Attorney General (NMAG)

Agency Analysis was Solicited but Not Received From
Taxation and Revenue Department (TRD)

SUMMARY

Synopsis of House Bill 326

House Bill 326 (HB326) creates the small business disaster relief income tax credit which allows a small business in a governor-declared disaster area to claim a $5,000 refundable tax credit. To qualify for the credit, a business must be in an area designated by the governor as a disaster area, and:

- Have been in business for at least two taxable years prior, including the year of the claim.
- Have had “annual gross revenue” below $2 million in that taxable year.
- Have experienced a 30 percent decline in gross revenue due to the disaster.

The bill requires the Economic Development Department (EDD) to certify the taxpayer.

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 provisions of the bill apply to tax years beginning 2025.

FISCAL IMPLICATIONS

This bill creates 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.

This analysis uses business establishment data from the Bureau of Labor Statistics' Quarterly Census of Employment and Wages to estimate the number of businesses who could benefit from HB326. This data reports the number of establishments by the number of employees and reports the total wages of these establishments.

First, this analysis estimates the number of businesses with annual revenue of $2 million or less. This analysis uses the total wages to simulate gross revenue by assuming a share of revenue that goes to support employment. Using this methodology, this analysis estimates that about 87 percent of businesses with nine or fewer employees have annual gross receipts less than $2 million, totaling 44.4 thousand business that meet the first prong of the bill's four-pronged eligibility criteria.

Second, this analysis estimates the number of these businesses who are in areas that face disaster risk. In 2023, the Energy, Minerals, and Natural Resources Department (EMNRD) published the *Communities at Risk Assessment Plan*, based on Community Wildfire Protection Plans. In that assessment, the agency concluded that 82.8 percent of communities face a moderate or high risk of wildland fire. Using that assessment, of the businesses who meet the first prong of eligibility criteria, about 36.8 thousand are also in communities that face moderate or high wildland fire risk. Wildland fire is not the sole risk communities face, meaning this estimate may underestimate the total true fiscal impact.

Third, this analysis estimates the share of these businesses are in areas that will be declared a disaster by the governor. From FY22 to FY24, the governor issued 450 executive orders, of which 371 (82 percent) declared disasters. This analysis estimates that these disasters spanned 50 discrete areas, although some regions had multiple emergency declarations over that period (i.e., due to the South Fork and Salt Fires). On average, this translates to an average of approximately 15 areas that were declared a "disaster area" per year. See *Significant Issues* for discussion of this terminology. Generally, these declarations refer to the county in which the emergency is taking place, meaning about 45 percent of counties on average had an emergency declaration.

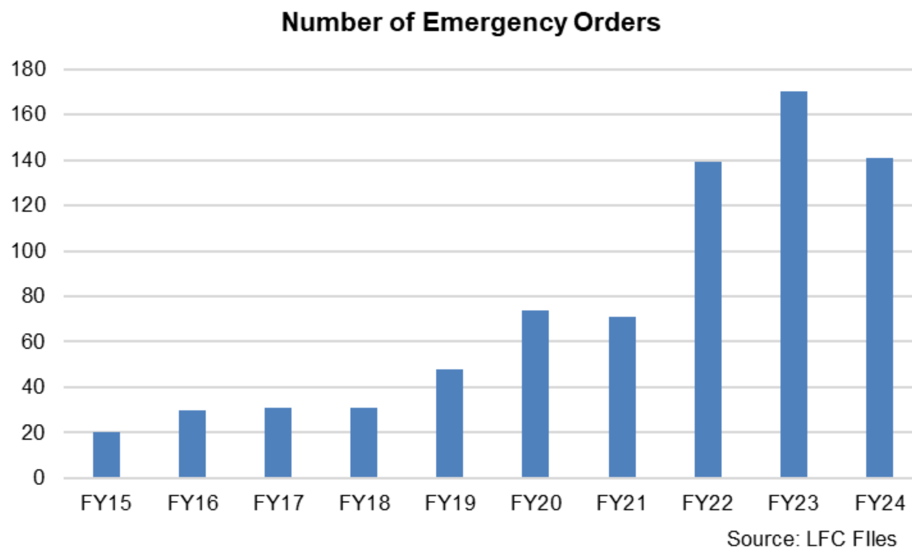
Lastly, this analysis estimates the share of those businesses that will see a 30 percent decrease in gross revenues because of a disaster that triggers a disaster declaration. The economic impact of natural disasters like wildfires and flooding is vast, but the specific impact on business revenues is challenging to estimate but likely very significant. Some businesses are far more susceptible to sudden, dramatic downturns because of a local natural disaster, including retail, accommodation,

and food services which make up about 20 percent of businesses. This analysis assumes 90 percent of these businesses and 5 percent of all other businesses could face a 30 percent decrease in gross revenues because of a natural disaster in a year.

Using these assumptions, this analysis assumes that about 3,800 small businesses in regions designated as "disaster areas" by the governor could see a 30 percent decline in revenue in any given year. This is about 7 percent of all businesses with less than nine employees. Assuming businesses maximize profits and uptake is uniform, total cost could be $19 million per year.

Risks. The bill's impact could far exceed the cost presented in this analysis. Consider the pandemic, wherein the governor declared a series of public health emergencies that would invoke the standards created by HB326. One survey estimated that 43 percent of small businesses closed just several weeks after the pandemic's onset. Under HB326, the state would be responsible for at least $150 million in credit payments, an over eightfold increase in the average expected annual costs. This would occur concurrently with a significant economic downturn that could sharply impact revenues, potentially causing a situation in which the state is unable to pay businesses without entering a deficit.

Emergency orders have proliferated in recent years. This analysis uses data from FY22 to FY24 to estimate potential impacts. However, should disaster-related emergency orders continue to grow, the impact could be significantly higher.



Operating budget impact. This analysis assumes EDD would need to add at least three new personnel (FTE) to meet the administrative burden created by HB326. The operating budget impact on page one assumes three new FTE at the agency's current average total compensation, for a recurring operating budget impact of $416 thousand per year. This analysis estimates about 3,800 businesses could qualify and apply for the credit each year. Assuming each application takes one hour of staff time to review, this would add 1.8 full-time equivalent staff hours of work each year. Additional staff resources would be required to stand up the program, respond to public questions, and coordinate with state agencies.

HB326 contemplates creating a potentially complex review process, but EDD analysis did not note the potentially significant administrative burden this would place on the agency. Without a thorough review, there could be an increase in fraudulent claims being approved, especially in situations where a business is in a disaster area but did not face a revenue decline because of the disaster. Additionally, EDD would likely be unable to process the volume of applications if there were a widespread emergency, like the pandemic, impacting the timeliness of credit processing.

Additional information about the administrative burden may be updated after receipt of analysis from the Taxation and Revenue Department (TRD).

SIGNIFICANT ISSUES

There are several significant issues with the legislation. First, the bill does not define a “disaster area.” The legislation may intend to only allow businesses in the immediate geographical area of a natural disaster to qualify. However, the legislation could intend to allow all businesses throughout a county to qualify if any part of that county received an emergency declaration. The term “disaster area” is not defined elsewhere in statute.

Similarly, the bill does not appear to align with the process by which the governor can use emergency powers. The governor’s emergency powers are defined in Chapter 12, Articles 10, 10A, 11 and 12 NMSA 1978. These sections of statute define clearly the powers conferred to the governor in the case of a “man-made or natural disaster causing or threatening widespread physical or economic harm that is beyond local control,” that requires state intervention. This analysis assumes the bill intends on invoking this section of law, but it does not do so explicitly. Implementation may be piecemeal, or even unworkable, unless it is specified.

Analysis from the New Mexico Attorney General (NMAG) notes:

> Section 1(C)(1) provides that “to be eligible for the credit, the taxpayer shall be an owner of a business that: (1) is located in an area declared by the governor as a disaster[.]” Utilizing the word “located” does not necessarily encompass a commonly used phrase in business law: “principal place of business.” By utilizing the word “located,” Section 1(C)(1) does not address a scenario where an LLC’s registered office address is physically located in a disaster zone, but the business operations are not impacted by the disaster. However, Section 1(C)(3) partially addresses this by requiring an eligible business owner to demonstrate a 30 percent decline in gross revenue.

The agency suggests a potential amendment to clarify this language. See *Technical Issues.*

The bill contemplates offering a $5,000 credit for impacted businesses. To meet the credit’s criteria, the business could have experienced up to a $600 thousand reduction in annual gross revenues. Few businesses have the necessary cash on hand to sustain this kind of impact without enacting layoffs or closures. The timing of the $5,000 credit may also be too late to prevent closures or layoffs. On the other hand, the $5,000 thousand credit may exceed revenue lost due to a disaster. A very small business with annual gross revenue equal to $10 thousand may experience a revenue decline of $3,000. The credit under HB326 would provide a windfall of $2,000 more than actual business losses.

NMAG analysis notes that HB326 requires a business to "demonstrate that it has sustained a 30 percent decline in gross revenue due to the disaster," but that the term "demonstrate" does not "provide uniform metrics that can be routinely reference by the individuals charged with assessing the requests for the tax credit."

The Economic Development Department (EDD) analysis of the bill notes that the credit must be claimed in the taxable year in which the disaster occurs. "In cases where a disaster is declared late in the taxable year," the agency writes, "businesses may not experience the full financial impact, including the 30 percent revenue decline, until the following year." This may reduce the benefit to business owners, the agency notes.

TECHNICAL ISSUES

NMAG notes:

> Section 1(G), as currently written, only applies to "a business entity that is taxed for federal income tax purposes as a partnership or limited liability company[.]" Partnerships and LLCs do not pay entity-level tax; rather, the business income passes through to the owners and is reported on the owner's individual tax returns. Notably S-Corporations can elect to be taxed like partnerships. Section 1(G) did not include business entities structured under Subchapter S of the Internal Revenue Code (even though they can be taxed like the partnership entity referenced in Section 1(G)). Accordingly, the effect of Section 1(G) is unclear.

The agency also suggests that policymakers consider the following amendment:

> Change "an area declared as a disaster area by the governor" to "an area in which the governor has proclaimed that a state of disaster or state of emergency exists."

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 the 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	

BG/hj/SR