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	3/20/2025
SPONSOR	Ramos/Sanchez/Block/Thornton	**ORIGINAL DATE**	3/3/2025
SHORT TITLE	No Armed Forces Retirement Tax Exempt Limit	**BILL NUMBER**	Senate Bill 497
		ANALYST	Gray

REVENUE*
(dollars in thousands)

Type	FY25	FY26	FY27	FY28	FY29	Recurring or Nonrecurring	Fund Affected
PIT	$0	$0	($5,000.0)	($5,200.0)	($5,400.0)	Recurring	General Fund

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

Sources of Information
LFC Files

Agency Analysis Received From
Department of Veterans' Affairs

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

SUMMARY

Synopsis of Senate Bill 497

Senate Bill 497 (SB497) increases the personal income tax exemption for armed forces retirees and surviving spouses of armed forces retirees from $30 thousand per year to the entirety of the taxpayer's income.

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 2026.

FISCAL IMPLICATIONS

This bill expands a tax expenditure that is estimated to reduce recurring general fund revenue by $5 million beginning in FY27. 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.

The Taxation and Revenue Department (TRD) provided the estimated revenue impact of SB497.

> The Statistical Report on the Military Retirement System provides an aggregate number of retirees (officers and enlisted) and survivor beneficiaries by state and an aggregate amount of benefits distributed. As of September 30, 2022, New Mexico had 20,257 reported retirees and 2,703 survivor beneficiaries. Aggregate annual distribution of military retirement benefits for retirees and survivor was approximately $635 million. This analysis assumes all retirees were qualified by years of service or disability to receive lifetime benefits.
>
> TRD used a Monte Carlo simulation to estimate the fiscal impact for officers and enlisted retirees and survivors with armed forces retirement income over $30 thousand. Officer retiree income constitutes the majority of the fiscal impact as the monthly average armed force retiree income is approximately $4,280. For enlisted retirees, the average monthly armed forces income is $2,110 and $1,326 for survivors. TRD calculated the aggregate fiscal impact to the state by multiplying the aggregate income over $30 thousand by an effective tax rate of 2.8 percent. Tax & Rev then inflated the annual impact by the Congressional Budget Office's inflation forecast to account for cost-of-living adjustments for military retirees.

Because detailed information on this population is not available at this time, the provisions of SB497 represent a risk to general fund revenue. The assumptions made in this analysis may not reflect the full extent of the costs of increasing the exemption.

SIGNIFICANT ISSUES

Horizontal equity is a core tenet of tax policy that holds that taxpayers with similar income and circumstances should be treated similarly under the tax code. This provision erodes that principle by favoring some taxpayers with the same income because the source of their income is from military retirement benefits. Policymakers may tolerate or approve of such a horizontal disparity if they believe the benefits of providing a tax benefit for military retirees outweigh the costs of a less horizontally equitable overall tax code.

There is no cliff effect for military retirees in the current tax code because all beneficiaries with military retiree income can currently claim an exemption. The amount of military retirement income above $30 thousand is subject to state income tax at the state marginal rate. The benefit contemplated by SB497 would only benefit retirees with income above $30 thousand per year, typically officers who serve for longer periods. According to the *Statistical Report on the Military Retirement System,* in New Mexico retired officers receive $51 thousand annually in retirement benefits, on average, while retired enlisted members receive $25 thousand annually in retirement benefits, on average.

Policymakers may consider many factors when deciding whether to exempt all military retirement income, including providing financial relief for that population, recognizing taxpayers' military service, and trying to attract military retirees to the state. The provisions of SB497 may have a limited impact on attracting military retirees to the state in part because this exemption is just one among a tapestry of tax policies that may make New Mexico attractive or unattractive for a retiree. For example, New Mexico's property taxes are among the lowest in the nation, but the state has a relatively high sales tax.

Analysis from the Department of Veterans' Services notes that the agency will provide outreach services to ensure the veteran community is fully informed about the increased exemption amount.

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 bill has not been 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 a clearly stated purpose, long-term goals, or measurable annual targets
Transparent: The tax expenditure requires at least annual reporting by the recipients, the Taxation and Revenue Department, and other relevant agencies	×	This bill does not require annual reporting.
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	×	This bill does not have 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 bill is effective and efficient, in part because the bill lacks targets.
Efficient: The tax expenditure is the most cost-effective way to achieve the desired results.	?	
Key: ✓ Met × Not Met ? Unclear		

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