F I S C A L I M P A C T R E P O R T

SPONSOR Ingle **ORIGINAL DATE** 2/2/16
LAST UPDATED **HB**

SHORT TITLE CYFD Community Home Donation Tax Credit **SB** 107

ANALYST Graeser

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY16	**FY17**	**FY18**	**FY19**	**FY20**		
	($2,210.1)	($2,312.1)	($2,439.1)	($2,556.1)	Recurring	General Fund (PIT)

Parenthesis ( ) indicate revenue decreases

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY16	FY17	FY18	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
Total	$47.7	$16.7	$16.7	$81.1	Recurring	TRD operating

Parenthesis ( ) indicate expenditure decreases

SOURCES OF INFORMATION
LFC Files

Responses Received From
Taxation and Revenue Department (TRD)
Children, Youth and Families Department (CYFD)

SUMMARY

Senate Bill 107 establishes a **refundable** income tax credit for cash donations to entities that operate facilities licensed by the Children, Youth and Families Department as community homes, establishes the guidelines for taxpayer eligibility to claim this credit, and limits the credit to **lesser** of fifty percent of the total amount of cash donations made by the taxpayer during the taxable year or two thousand five hundred dollars.

The credit can be claimed in the year in which the cash donation is made and can only be deducted from the taxpayer's income tax liability with any excess refunded to the taxpayer. The taxpayer is required to provide the Taxation and Revenue Department (TRD) adequate documentation to support the credit. TRD shall not allow the credit if on the date of the department's receipt of the taxpayer's claim for credit the total amount of credits allowed for donations made to the entity during the calendar year of the taxpayer's donation exceed the product of $50 multiplied by the total number of residential care days attributable to the entity during the same calendar year.

The bill further provides that the taxation and revenue department shall allow the community home donation tax credit if the taxpayer submits satisfactory evidence that the taxpayer made a cash donation and that on the date of the cash donation, the entity held an active, valid community home license issued by the CYFD.

There is no effective date of this bill. It is assumed that the new effective date is 90 days after this session ends (May 18, 2016). The provisions of the act apply to taxable years beginning on or after January 1, 2016.

FISCAL IMPLICATIONS

"TRD used federal and state income tax data extracted from federal schedules for tax year 2013 data to estimate the fiscal impact. Included in the data was the number of charitable contributors as well as the total dollar amount of charitable contributions. In accordance with the language of the bill the maximum credit is $2,500; a contribution of $5,000 or more maximizes the credit. The average contribution calculated from 2013 tax data is $4,603, resulting in an average tax credit of $2,302."

"The most significant assumption affecting the fiscal impact is the percentage of contributors that would donate to a qualifying community home. TRD assumes that 0.5% of all contributors donates, or would donate, to a qualifying entity. This assumption calculated a baseline tax year 2013 estimate. The PIT growth rates from the December 2015 consensus estimate were applied to quantify the out-year fiscal impact."

This bill may be counter to the LFC tax policy principle of adequacy, efficiency and equity. Due to the increasing cost of tax expenditures revenues may be insufficient to cover growing recurring appropriations.

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 expenditure's 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.

SIGNIFICANT ISSUES

TRD notes that, "This bill implicates the tax policy principle of efficiency and is designed to incentivize public investment in community homes that are licensed by CYFD. These types of homes provide valuable services and can lessen government burdens. However, consideration should be given to the interrelationship between federal income tax law and New Mexico income tax law, depending on the character of the entities that operate group homes. If these entities are non-profit entities, a portion of the contribution would be deductible under federal law, thereby reducing the taxpayer's New Mexico tax base. Allowing an additional 50% credit for the donation, when at least a portion of the donated amount is untaxed by New Mexico, may create a double benefit. As such, in this instance it might be prudent to consider whether a refund provision, rather than a carryforward, is necessary. Additionally, substantiating charitable donations is problematic for the IRS. These challenges will extend to New Mexico vis-à-vis audit and compliance obligations and there is potential for abuse, especially with a refundable credit."

It is very unusual for this type of tax credit to be refundable, without reference to tax liability. There is some concern that this refundability may violate the anti-donation clause of the constitution (Article IX, Section 14). This bill provides for cash paid by the state in aid of a private individual. If the credit were non-refundable, then the provisions of this bill would be adjusting the tax liabilities of individuals based on the legislature's constitutional prerogative to subsidize certain behaviors and actions deemed to be in the public interest through the tax system.

Article IX, Sec. 14 of the New Mexico Constitution provides as follows:
"Neither 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 or in aid of any private enterprise for the construction of any railroad except as provided in Subsections A through G of this section.

A. Nothing in this section prohibits the state or any county or municipality from making provision for the care and maintenance of sick and indigent persons."

There is no aggregate cap on amounts of donations.

This may be a "double dip" if the licensed community home is a non-profit entity. Then the full amount of donation can be deducted from federal and state income tax returns and result in tax savings of, typically, 30% to 35% of the amount of the donation. This state tax credit is in addition to the value of the deduction.

PERFORMANCE IMPLICATIONS

The LFC tax policy of accountability is <u>not</u> met since TRD is <u>not</u> required in the bill to report annually to an interim legislative committee regarding the data compiled from the reports from taxpayers taking the deduction and other information to determine whether the deduction is meeting its purpose. Nor is the purpose of the credit clear. It may be that the intent is to increase remuneration to operators of community homes over and above the amount of reimbursement from CYFD. Or it might be that CYFD has difficulty in obtaining operators of community homes. However, CYFD indicates that there are currently seven homes licensed by CYFD which fall into this category.

ADMINISTRATIVE IMPLICATIONS

TRD notes a moderate impact:

"New forms and instructions will be required. IT systems will need to be updated and configured to support the credit."

"A quarter FTE is necessary to administer this credit. Policies and procedures to coordinate with community homes and ascertain claimant eligibility as prescribed in the bill are necessary. If we rely upon the claimant to provide the requisite information, the FTE requirement may increase as the process will be more challenging."

TECHNICAL ISSUES

TRD notes that, "…the bill proposes language for eligibility that creates challenges for both taxpayers and TRD. Taxpayers have neither access to total number of care days information, nor knowledge of the entity's license status (as of the date of the donation). Moreover, this creates a cumbersome validation requirement for TRD; adjudicating eligibility is onerous. At a minimum a pre-approval process would be necessary and coordination with CYFD should be statutorily authorized. CYFD could greatly assist in administration of this credit by publishing and periodically updating lists of licensed facilities in good standing. The other technical issue is with the annual cap. Because it changes, potentially frequently, depending on the number of licensed facilities, it constitutes a moving cap. Moving caps require disproportionately large expenses for the value they provide. It would be far more simple and cleaner to set an aggregate dollar value cap and require a review each year or every other year to accommodate the changing number of licensed facilities."

This bill does not contain a delayed repeal date. The LFC recommends adding a delayed repeal date.

OTHER SUBSTANTIVE ISSUES

TRD notes, "…no impact to the financial distribution business processes. However, the credit may be subject to the financial statement disclosure requirements per GASB Statement No. 77. GASB 77 disclosure requirements are effective for financial statements for periods beginning after December 15, 2015. An assessment of the credit against the tax abatement criteria specified in GASB 77 would need to be performed by TRD. If the credit meets the tax abatement criteria, then disclosure would be required in TRD's financial statements for the fiscal year ending June 30, 2017. Tax Policy would need to provide the Financial Distribution Bureau (FDB) with the assessment and note disclosure for financial reporting and external audit purposes. Estimated FDB time impact – 8 hours or less"

Does the bill meet the Legislative Finance Committee tax policy principles?

1. **Adequacy**: Revenue should be adequate to fund needed government services.
2. **Efficiency**: Tax base should be as broad as possible and avoid excess reliance on one tax.
3. **Equity**: Different taxpayers should be treated fairly.
4. **Simplicity**: Collection should be simple and easily understood.
5. **Accountability**: Preferences should be easy to monitor and evaluate

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