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

		LAST UPDATED	
SPONSOR	Jaramillo	**ORIGINAL DATE**	2/4/24
SHORT TITLE	Calf Canyon Fire Legal Svcs. Gross Receipts	**BILL NUMBER**	Senate Bill 174
		ANALYST	Torres, Ismael

REVENUE*
(dollars in thousands)

Type	FY24	FY25	FY26	FY27	FY28	Recurring or Nonrecurring	Fund Affected
GRT		($7,000.0) to ($12,480.0)	($9,000.0) to ($9,930.0)	($4,960.0) to ($9,000.0)		Recurring	General Fund
GRT		($4,700.0) to ($8,520.0)	($6,000.0) to ($6,780.0)	($3,390.0) to ($6,000.0)		Recurring	Local Governments

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

Sources of Information

LFC Files
FEMA Calf Canyon Update

Agency Analysis Received From
Taxation and Revenue Department (TRD)
New Mexico Attorney General (NMAG)
Department of Homeland Security and Emergency Management (DHSEM)

SUMMARY

Synopsis of Senate Bill 174

Senate bill 174 (SB174) provides a gross receipts tax deduction for the sale of legal services, "rendered to and at the request of a person eligible to receive compensation pursuant to the federal Hermit's Peak/Calf Canyon Fire Assistance Act," so long as those legal services are directly related to the person receiving compensation.

The effective date of this bill is July 1, 2024.

FISCAL IMPLICATIONS

This bill creates a tax expenditure with a cost that is difficult to determine but likely significant. LFC notes the risk to state revenues from tax expenditures and the increase in revenue volatility from erosion of the revenue base. The committee recommends bills adhere to the LFC tax expenditure policy principles for vetting, targeting, and reporting or action be postponed until the implications can be more fully studied.

The federal Hermit's Peak/Calf Canyon Fire Assistance Act provides $3.95 billion to compensate claimants impacted by the Hermit's Peak/Calf Canyon Fire. The estimates on page one approximate about 90 percent of the available compensation is recovered through an attorney's services, due to the experience of the Fire Victim Trust in California which exhibited such service utilization rates. Further, the analysis assumes 20 percent attorney fees, as is limited in the federal act.

According to the Federal Emergency Management Agency (FEMA) website, $311 million has already been paid in compensation as of Jan. 11, 2024, with another $1 billion expected to be paid by Jan. 1, 2025. The remainder of the funds are assumed to be paid out over the following two years as claims must be submitted no later than November 14, 2024, and November 14, 2025, for amended claims. Additionally, FEMA has an overall 180-day timeline to make compensation determinations.

Given those amounts and timelines, LFC staff used an effective statewide GRT rate of 7.03 percent and an effective state general fund rate of 4.18 percent to estimate the impacts of SB174. The estimates from the Taxation and Revenue Department using a similar analysis is the basis for the range when compared with LFC estimates.

SIGNIFICANT ISSUES

This bill narrows the gross receipts tax (GRT) base. Many New Mexico tax reform efforts over the last few years have focused on broadening the GRT base and lowering the rates. Narrowing the base leads to continually rising GRT rates, increasing volatility in the state's largest general fund revenue source. Higher rates compound tax pyramiding issues and force consumers and businesses to pay higher taxes on all other purchases without an exemption, deduction, or credit.

The Taxation and Revenue Department highlights:

> This deduction though erodes horizontal equity in GRT taxes as it treats claimants of the Hermit's Peak/Calf Canyon Fire as unique from other taxpayers who have suffered losses from fires, flooding, or other natural disasters. While tax incentives may support particular industries or encourage specific social and economic behaviors, the proliferation of such incentives complicates the tax code. Adding more tax incentives: (1) creates special treatment and exceptions to the code, growing tax expenditures or narrowing the tax base, with a negative impact on the general fund; and (2) increases the burden of compliance on both taxpayers and TRD. Adding complexity and exceptions to the tax code does not comport generally with the best tax policy.
>
> A key policy issue is that tax deductions may not be applied retroactively. As payments under the Act have already started, legal fees incurred prior to the effective date of this bill would have been subject to GRT. Because gross receipts taxes are due on a monthly basis, in most cases, the tax would already have been paid. Under the New Mexico Constitution, and applicable case law, a tax deduction may not be retroactive. Therefore, the proposed tax deduction for the sale of legal services directly related to recovering compensation for individuals who were eligible to receive compensation from the Act can only apply to receipts received on or after the effective date of this bill.

Taxpayers choose which deductions to claim and are not required to claim a deduction just because it is available to them. For example, after recent enactment of a new GRT deduction for feminine hygiene products, TRD received complaints that some retailers were still charging GRT on those products. It is possible that some lawyers will not claim the deduction and will continue to pass GRT along to their clients on the services rendered.

GRT rests upon the general presumption that all receipts of a person engaged in business in New Mexico are subject to the GRT and that this rate represents the rate upon which the State collects taxes on transactions.1 GRT represents the largest recurring revenue source for the state general fund at around 34 percent, about 80 percent of municipal revenue, and 30 percent of county revenue.

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.	×	
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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