BILL ANALYSIS AND FISCAL IMPACT REPORT
Taxation and Revenue Department

February 24, 2025

Bill: HB-325 **Sponsor:** Representatives Gail Armstrong, Mark Duncan, Mark B. Murphy, Rebecca Dow and Joshua N. Hernandez

Short Title: Home Construction Tax Credit

Description: This bill creates two new gross receipts tax (GRT) deductions. Section 2 provides a deduction from gross receipts from selling labor incurred during the construction of new residential housing. Section 3 provides a deduction of up to $125,000 during a twelve-month period for the sale of new residential housing, or $75,000 during any twelve-month period from the sale of new residential housing intended for lease. Provisions are included in Sections 2 and 3 to prevent a taxpayer from taking both deductions. The bill also creates a 100% hold harmless distribution to municipalities and counties for these two new deductions.

Effective Date: July 1, 2025

Taxation and Revenue Department Analyst: Pedro Clavijo

Estimated Revenue Impact*					**R or NR****	**Fund(s) Affected**
FY2025	**FY2026**	**FY2027**	**FY2028**	**FY2029**		
--	($21,600)	($22,400)	($22,700)	($22,800)	R	Section 2: General Fund
--	($23,400)	($24,200)	($24,600)	($24,700)	R	Section 2: Local Governments
--	($22,700)	($23,600)	($23,900)	($24,100)	R	Section 3: General Fund
--	($24,600)	($25,600)	($25,900)	($26,100)	R	Section 3: Local Governments
--	($48,000)	($49,800)	($50,500)	($50,800)	R	Section 1: General Fund – Hold Harmless Distributions
--	$48,000	$49,800	$50,500	$50,800	R	Section 1: Local Governments – Hold Harmless Distributions
--	$0	$0	$0	$0	R	**Total – Local Governments**
	($92,300)	($95,800)	($97,100)	($97,700)	R	**Total – General Fund**

* In thousands of dollars. Parentheses ( ) indicate a revenue loss. ** Recurring (R) or Non-Recurring (NR).

Methodology for Estimated Revenue Impact: [Section 2:] The Taxation and Revenue Department (Tax & Rev) used the University of New Mexico's Bureau of Business and Economic Research (BBER) January 2025 forecast on total housing units authorized in New Mexico and the statewide median price of sold units through December 2024 to compute the fiscal impact of deducting receipts from selling labor to construct new residential housing. Then, Tax & Rev assumed that labor costs of residential construction are around 27.5% of the total cost.[1] The analysis is based on a statewide effective GRT rate. The fiscal impact includes the effects of this deduction on the 1.225% distributions to municipalities pursuant to Section 7-1-6.4 NMSA 1978 as the majority of construction is assumed to be in municipalities.

[1] Labor vs material cost in construction: Overview - Bridgit

[Section 3:] Tax & Rev used BBER's forecast on total housing units authorized in New Mexico as a proxy for the sale of new residential housing. Since Tax & Rev cannot predict the number of new residential housing units sold that are intended for lease (see Technical Issues), Tax & Rev used an average deduction of $100,000 taxpayers might claim under this section. The analysis is based on a statewide effective GRT rate. The fiscal impact includes the effects of this deduction on the 1.225% distributions to municipalities pursuant to Section 7-1-6.4 NMSA 1978 as the majority of construction is assumed to be in municipalities.

Tax & Rev cannot predict whether the proposed deductions will be enough to stimulate the construction of new housing projects and place the State above its current trend, so the analyses assume the forecasted trajectory under BBER's current housing construction forecast.

[Section 1:] The hold harmless distributions are the sum of the local governments' impacts under Sections 2 and 3, including the 1.225% stipulation under subsection A, on page 2 which offsets the loss for municipalities under 7-1-6.4 NMSA 1978.

Policy Issues: The residential housing system in the US, in general, and in New Mexico in particular, faces several significant challenges when it comes to cost. These challenges are interconnected and impact affordability, accessibility, and the overall stability of the housing market. One of the main drivers of high home prices is the lack of available housing supply. There are not enough homes being built to meet the demand. This is due to a combination of factors, including restrictive zoning laws, a shortage of skilled labor in construction, and rising costs of labor and materials. When supply does not keep up with demand, prices inevitably rise. High home prices are closely tied to increasing rents. Median rents in New Mexico increased by 60% from 2017 to 2024, much more than the 27% recorded for the US overall. The average price of a New Mexico home climbed even faster during that time, increasing by 70%. High prices have forced individuals to live in substandard conditions or face high rental rates that drain their incomes. The limited rental supply has made it even more difficult for low-income and middle-class families to find affordable housing. From 2017 to 2024, homelessness in New Mexico increased by 87%, more than double the nation's 40% rise.[2] Thus, the proposed deductions might help increase the number of units and revert the troubling trend of the housing system across New Mexico.

While tax incentives can support specific industries or promote desired social and economic behaviors, the growing number of such incentives complicate the tax code. Introducing more tax incentives has two main consequences: (1) it creates special treatment and exceptions within the code, leading to increased tax expenditures and a narrower tax base, which negatively impacts the general fund; and (2) it imposes a heavier compliance burden on both taxpayers and Tax & Rev. Increasing complexity and exceptions in the tax code is generally not in line with sound tax policy. As noted under technical issues, these deductions will present several more options to taxpayers in the residential housing market. Without clear language in the statute, as to any ordering of taking deductions, local governments may not see the full hold harmless payments matching overall deductions taken in the taxing district as taxpayers will determine the most advantageous deductions to apply. The complexity of deductions for residential construction will require additional outreach and education for taxpayers and more complex auditing of compliance.

Finally, legislation should seek to ensure that the benefit of this deduction be reflected in lower housing prices and not absorbed by businesses themselves. Businesses might take the deductions or see their construction labor costs reduced, but still charge a final price for a new house in line with a tight housing market with no impacts on affordability or the median home price. The final effect of this bill is not clear.

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[2] Restrictive Regulations Fuel New Mexico's Housing Shortage | The Pew Charitable Trusts

The deduction does not have a defined sunset date. Tax & Rev supports sunset dates for policymakers to review the impact of tax expenditures before extending them.

Technical Issues: [Section 2] Under this proposal it is unclear as to by whom the labor is being performed, and to whom the labor is being sold. The GRT is imposed on the seller, and generally passed on to the purchaser. A housing developer may purchase labor services from other companies, making the deductions available for different taxpayers. A subcontractor may be providing the labor services through a prime contractor, in which case the subcontractor could take this deduction under Section 2, while the prime contractor and seller of the completed residence could take the deduction under Section 3. It is not clear whether this is the intent of the bill. The bill also overlaps with Section 7-9-52 NMSA 1978, which already permits a person selling construction services to a person engaged in the construction industry to deduct their receipts, so long as the subsequent sale of the completed construction project is taxable (which mirrors the requirement in Section 7-9-48 NMSA 1978, which allows a seller of services sold for resale to deduct those receipts, so long as the subsequent sale is subject to gross receipts tax). If the deduction in Section 2 may be taken by subcontractors who provide labor to prime contractors constructing residential housing, then that subsequent sale of the residence should be required to be subject to gross receipts tax. Alternatively, the bill could require subcontractors to take any deduction under Section 7-9-48 rather than taking this new deduction.

[Section 3]: The deduction amount under section 3 has two amounts under subsection A. (1) and (2) on page 4, $125 thousand for the sale of a new “residential housing” and $75 thousand for the sale of new “residential housing” intended for lease. Tax & Rev notes two concerns with the proposed language. The taxpayer selling residential housing may not have knowledge or control over the intended use of the new housing whether it is for owner-occupied or for future rent. Furthermore, there is no requirement that the completed housing actually be leased, whatever the initial intent was. There is no way for Tax & Rev, or the person performing the construction, to verify intent or whether that intent was fulfilled. This is particularly the case for single-family residence, a town house or a condominium. Secondly, a home intended for lease would still qualify under the requirement in subsection A (1) as it places no restriction on the home being owner-occupied. Tax & Rev suggests one deduction amount so as to not incentivize one particular type of new residential housing and ease the administrative burden on taxpayers and Tax & Rev.

Other Issues: None.

Administrative & Compliance Impact: Tax & Rev will update forms, instructions, and publications. As noted under Policy Issues, the additional complexity of GRT deductions in the residential construction industry will require taxpayer outreach and education. Tax & Rev will need to have expanded staff training to ensure compliance.

Implementing this bill will have a moderate impact on Tax & Rev’s Information Technology Division (ITD), approximately 700 hours or about four and a half months and $161,000 in contractual costs. Tax & Rev’s Administrative Services Division (ASD) anticipates implementing the bill will take 100 hours and two existing FTEs and cost $6,300 in staff workload.

Given the administrative impact of implementing this proposal, Tax & Rev suggests an effective date of January 1, 2026.

Estimated Additional Operating Budget Impact*				R or NR**	Fund(s) or Agency Affected
FY2025	FY2026	FY2027	3 Year Total Cost		

--	$6.3	--	$6.3	NR	ASD – Staff Workload
$161	--	--	$161	NR	ITD - Contractual costs

* In thousands of dollars. Parentheses ( ) indicate a cost saving. ** Recurring (R) or Non-Recurring (NR).