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

SPONSOR Maes **DATE TYPED** 2/13/04 **HB**

SHORT TITLE Amend Lab Partnership & Business Tax Credits **SB** 197/aSCORC

ANALYST Neel

REVENUE

Estimated Revenue		Subsequent Years Impact	Recurring or Non-Rec	Fund Affected
FY04	**FY05**			
	(2,400.0)	(2,400.0)	Recurring	General Fund
	*	*	Recurring	General Fund

(Parenthesis ( ) Indicate Revenue Decreases)

Duplicates HB 194, Amend Lab Partnership & Business Tax Credits

Relates to:
HB 67, High-Wage Jobs Tax Credit;
SB 28, High-Wage Jobs Tax Credit
SB 78, National Lab Water Treatment

SOURCES OF INFORMATION
LFC Files

<u>Responses Received From:</u>
Taxation and Revenue Department (TRD)
Economic Development Department (EDD)

SUMMARY

<u>Synopsis of SCORC Amendment #1</u>

The Senate Corporations and Transportation Committee amendment makes the following changes:

- Specifies that the combined small business and supplemental tax credits may not exceed $4.2 million;
- Deletes the $2.5 million small business credit annual floor amount mandated in the original proposal;

- Specifies that the proposed supplemental tax credit may only be claimed if the lab's claims for small business assistance do not exceed $2.5 million;
- States that the lab shall use the supplemental tax credit the same year the amount is calculated by the department; and
- Corrects a small technical error.

Synopsis of Original Bill

Senate Bill 197 amends the Laboratory Partnership with Small Business Tax Credit Act (LPSBTCA) to increase from $5 thousand and $10 thousand, to $10 thousand and $15 thousand, the credit amounts allowed in non-rural and rural areas, respectively. The statutory limit on the total amount allowed under the LPSBTCA is increased from $1.8 million per year to $4.2 million. Additionally, there is a new funding floor of $2.5 million. A supplemental tax credit is added in an amount equal to subtracting the gross receipts taxes paid in calendar year 2003 (base year) from gross receipts taxes due in subsequent calendar years, and multiplying by one-third. New reporting requirements are included in the legislation requiring quarterly and annual reports.

Significant Issues

The Legislature has consistently emphasized economic development and job creation. The 2003 Legislature renewed the job mentorship tax credit that encourages businesses to hire young people to participate in career preparation education programs by providing tax credits of up to 30 percent of the gross wages paid for employing young people; the credit is limited to 320 hours per student. The Investment Tax Credit Act (Chapter 402) was amended to reduce the employment requirements to qualify for the credit; it now allows tax credits equal to 5 percent of the value of qualified equipment purchased and incorporated into certain manufacturing operations in the state.

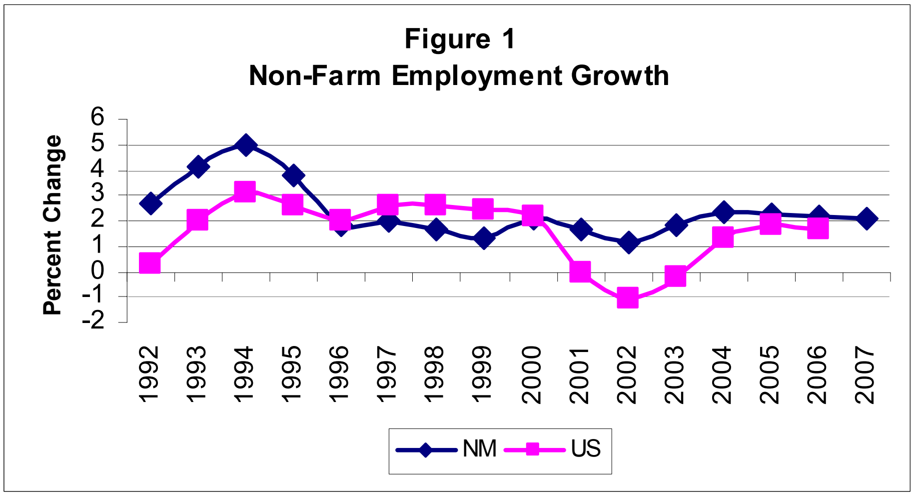
In 2002 the Legislature passed HB 40 *Software Development GRT Credit* (Laws 2002, Chapter 10) to provide a gross receipts tax deduction for receipts for software design and development and web-site design and development. The 2000 Legislature passed HB 19 *Technology Jobs Tax Credits* (Laws 2000, Chapter 22, 2nd SS) that provides a basic tax credit and an additional tax credit, both in the amount of 4 percent of the qualified expenditure made by a taxpayer conducting "qualified" research at a "qualified facility". To be eligible for the additional credit, the taxpayer must increase its payroll by $75.0 over the base payroll of the taxpayer for each $1.0 million of qualified expenditures.

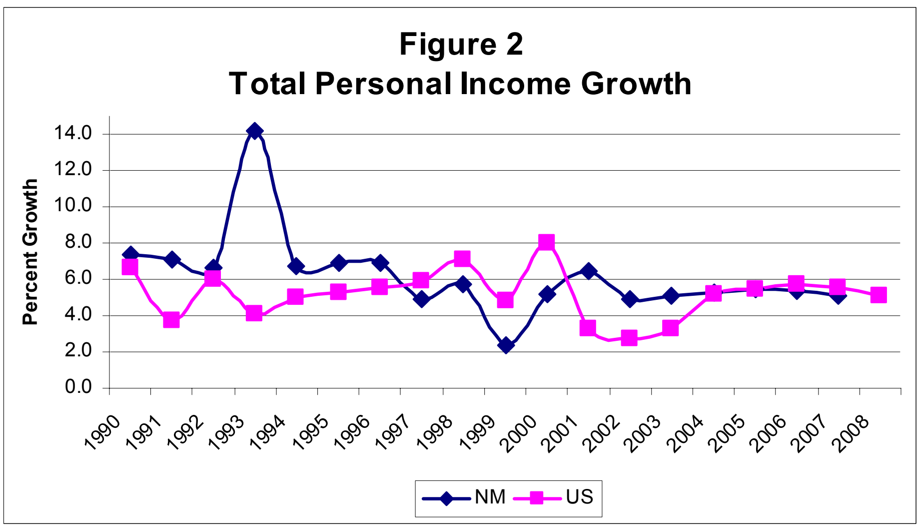
New Mexico Economic Performance. Two of the most vital indicators of a state's economy are its employment and income growth. Although these indicators are often influenced by external forces, the mission of the Economic Development Department remains to provide programs and policies that help lead the state in a direction that produces an overall benefit for the citizens of New Mexico.

Figures 1 and 2 graphically depict New Mexico's need to "promote increased employment and higher wages". As illustrated in Figure 1, New Mexico lagged behind the United States in nonagricultural employment growth from 1996 to 2000. When the United States economy slipped into a recession in 2001, 2002, and 2003, New Mexico sustained a modest rate of job growth and ranked among the fastest growing states.

Similar to employment growth, New Mexico maintained a higher personal income growth from 1991 to 1996 than that of the nation. Growth, again, began to decline in 1997 and fell behind the

United States. But in 2001 and 2002, New Mexico's growth surpassed the nation's, primarily due to the recession, as shown in the personal income growth graph.





FISCAL IMPLICATIONS

*TRD notes that confidentiality provisions of section 7-1-8 NMSA 1978 prohibit it from divulging individual taxpayer information. TRD notes that the fiscal impact associated with the supplemental tax credit will vary depending upon how much the lab's prospective annual GRT liabilities exceed the GRT paid in the base year. The amount will increase as business operations grow and expand.

TECHNICAL ISSUES

EDD makes the following content comments:

- "Reasonable Cost" should be defined. Also, EDD believes the intent of this legislation is to leverage national laboratory expertise for the purpose of providing direct, technical assistance to small business. Therefore, we question the usage of contractors. If the laboratory does not have the appropriate expertise, then it should refer the client company to a service provider that does.

TRD makes the following substantive comments:

TECHNICAL ISSUES: Proposed amendment number 3 does not provide a specific period in which the small business claims may not exceed $2.5 million for the purpose of qualifying for the supplemental tax credit. It is assumed the $2.5 million amount is the annual threshold. If this is the case "in a calendar year" should be inserted after "(2,500,000)".

OTHER IMPACTS AND ISSUES:

- As the original bill was written, it was not at all clear if the "supplemental tax credit" was in any way related to actual small business assistance provided by the laboratory. The SCORC amendment does link the two by specifying that the supplemental credit may only be claimed if the lab's small business claims are less than $2.5 million [in a given year]. The lab's small business claims are explicitly based on actual expenditures made to provide small business assistance. However, there is no similar criterion for the supplemental credit. ***Hence, it appears as if the supplemental credit actually rewards the lab for <u>not</u> providing small business assistance.*** Depending upon how much the lab's prospective GRT liabilities exceed the amount of GRT paid in the base year, the lab could provide assistance sufficient to qualify for and claim small business credit up to the $2.5 million threshold amount, then, without providing any additional assistance, claim the supplemental credit until the combined credit amounts total $4.2 million. The supplemental credit simply guarantees the lab some additional credit over the amount for which they would qualify for providing small business assistance alone.
- The laboratory may contract with qualified outside entities to aid in the provision of small business assistance. Thus the lab, rather than acting solely as a provider of technical assistance, is essentially an administrator of a state-funded assistance program. A direct appropriation to the relevant state agency for expenditure in this program *by contract*, would be a less expensive means of funding this program, and allow for greater oversight.
- This law has a single intended beneficiary. Targeting preferential tax treatment to specific businesses is not good tax policy. It increases complexity and sets a precedent that other businesses can use to obtain similar tax preferences.
- The bill requires businesses receiving assistance to certify that they couldn't obtain the same assistance at a reasonable cost from another New Mexico business. It further stipulates that the lab document due diligence to determine likewise, but it is not mentioned what types of documentation are acceptable. Further, the term "reasonable" is quite subjective and it is not clear who is responsible for determining reasonable cost.
- According to information provided by the national laboratory, technical assistance is provided to roughly 300 New Mexico small businesses annually, with average per-business spending of just over $4,000.

SN/yr