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

		ORIGINAL DATE	02/07/13		
SPONSOR	HEC	**LAST UPDATED**	03/01/13	**HB**	24/HECS
SHORT TITLE	College Endowment Contribution Gross Receipts			**SB**	
				ANALYST	Walker-Moran

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY13	**FY14**	**FY15**	**FY16**	**FY17**		
	($1,200.0)	($1,200.0)	($1,200.0)	($1,200.0)	Recurring	General Fund
	($800.0)	($800.0)	($800.0)	($800.0)	Recurring	Local Governments

(Parenthesis ( ) Indicate Revenue Decreases)

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY13	FY14	FY15	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
Total		$35.0	$35.0	$70.0	Recurring	TRD

(Parenthesis ( ) Indicate Expenditure Decreases)

SOURCES OF INFORMATION
LFC Files

Responses Received From
University of New Mexico (UNM)
Taxation and Revenue Department (TRD)
New Mexico State University (NMSU)
Economic Development Department (EDD)
Department of Finance and Administration (DFA)
Higher Education Department (HED)

SUMMARY

Synopsis of Bill

The House Education Committee substitute to House Bill 24 enacts a new section of the gross receipts and compensating tax act to create the technology transfer and commercialization or collaborative scientific research funding tax credit. A taxpayer may claim 50 percent of a distribution made to a New Mexico 4-year public post-secondary education institution or a designated nonprofit entity of such school specifically for technology transfer and commercialization or collaborative scientific research purposes or an eligible endowment fund or an organization that promotes the commercialization of licensed technology conceived in a New Mexico four-year public post-secondary educational institution or federal scientific and engineering laboratory or test facility located in New Mexico. The tax credit cannot exceed $500,000 in a given calendar year. The credit is capped at $2 million. An eligible endowment fund is defined in the bill.

The purpose of the tax credit provided by this section is to provide an incentive for the technology transfer and commercialization industry to locate and expand in New Mexico.

For the purpose of the credit eligible endowment fund, scientific research, and technology transfer and commercialization area defined.

The <u>effective and applicability date</u> of this bill is July 1, 2013. The provisions apply to GRT returns filed on or after August 1, 2013. There is no sunset date. The Legislative Finance Committee (LFC) recommends adding a sunset date.

FISCAL IMPLICATIONS

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.

This bill will further narrow the gross receipts tax base and would move New Mexico away from the tax policy goal of a gross receipts tax with a broad equitable base and a low rate.

According to the Taxation and Revenue Department (TRD), giving to educational institutions is highly variable and follows no clear trend. At the University of New Mexico (UNM), for example, New Mexico's largest four year public university, published audit reports show that non-operating revenue from gifts decreased by nearly 42 percent in FY12, after increasing by almost 77 percent in FY11. Given the large presence of national laboratories in New Mexico, and the relatively low aggregate annual cap, combined with the lack of an economic-theory based method of fiscal impact estimation, the fiscal impact is assumed to be the maximum $2 million annually, with 60 percent of the impact falling on the General Fund and 40 percent on local governments.

SIGNIFICANT ISSUES

The concept of providing incentives for technology commercialization was presented to the interim committees in the fall of 2012. The UNM and the Council of University President's support this concept. The funding mechanism devised by the committees provides an incentive for commercial entities (which pay gross receipts tax) to support the endowments with less impact to the General Fund than a direct appropriation.

According to the New Mexico State University (NMSU), this bill could have an impact to the degree that actual gifts would be made to such funds; it could have a positive impact on commercialization of technology, possibly providing additional funds any commercialization could generate. The direct benefit would come from the endowment itself. Approved activities funded with income from the endowment include: (1) recruiting and retaining faculty; (2) funding collaboration between universities and federal laboratories; and (3) engaging in technology research, development, and commercialization.

The NMSU also would benefit indirectly as the tax credit would encourage a larger and more robust entrepreneurial culture and economy in New Mexico. As the institution invests in and grows its incubator facilities and programs, the growth of prospective tenants and clients could increase the likelihood of success.

This bill provides dollars to existing technology development and commercialization efforts and initiatives. In addition, the funds are available to meet matching cost requirements of federal technology commercialization grants that the NMSU might aspire to apply for but do not because of the lack of matching funds. Income from the endowment would help fund existing programs plus provide access to initiatives which would be beneficial but are hereto for impractical to even apply for owing to matching requirements.

This bill supports technology based economic development mission of the NMSU to fund existing technology development commercialization programs and procedures. It increases the likelihood of applying for and securing federal grants for technology based economic development programs which currently are financially infeasible for the NMSU to even consider applying for.

As reported by the Economic Development Department (EDD): According to the Merriam-Webster dictionary: “contribution” has a broader meaning that may include the contribution of time, expertise or other in-kind donations related to voluntarily providing services as well as funds or personal property; and “distribution” is an actionable term indicating the transfer of funds or personal property. There is a clear intention in the substitute bill to limit the eligibility of the tax credit to providing funds, with no potential loophole for businesses that might contribute services or other in-kind donations. All of these changes are important to the economic growth of the state. Funding is a key component for early stage companies and new technologies must ultimately reach the private sector if they are to contribute to New Mexico’s economic growth and diversity.

As reported by the Higher Education Department (HED), the substitute bill allows distributions to qualified entities including organizations that promote the commercialization of licensed technology conceived in a public university or federal laboratories. That definition is sufficiently broad to include investment in private companies meeting those characteristics. Distributions to public entities could be considered donations, without expectation of recompense. Distributions to private business, on the other hand, often carry an expectation of some sort of return on that investment. Subsidizing private investment in private firms might be considered an unintended consequence of this legislation.

PERFORMANCE IMPLICATIONS

The LFC tax policy of accountability is met with the bill’s requirement to report annually to the LFC regarding the data compiled from the reports from taxpayers taking the deduction and other information to determine whether the deduction is meeting its purpose.

There is no mechanism to ensure that the educational institutions who are certifying donations with the TRD are reporting to the Legislature as required. Confidentiality restrictions would prohibit the TRD from disclosing this information.

ADMINISTRATIVE IMPLICATIONS

Regulations would be needed to determine approval and audit procedures. The bill provides little guidance. A plan to determine which contribution certificates are legitimate would be needed to avoid the potential for fraudulent claims. An application form and instructions would need to be developed at a cost of $4,000. Publications would need to be updated. GenTax and the internet e-file application would need to be modified to record the credit. Credits against gross receipts tax are difficult and awkward to manage with existing resources, so the credit would have to be managed manually until other applications can be built. One FTE at a cost of $35,000 would be needed to assist with managing and tracking the credit and the annual cap.

TECHNICAL ISSUES

The TRD will not be able to implement the GenTax modifications necessary to record and claim the tax credit until at least October 1, 2013, after the effective date of the legislation.

“Administer”, “promote” and “market”, “advise and assist” are very broad terms without specific explanation as to how these uses contribute to the creation of sustainable tech-intensive businesses that remain in New Mexico. The information required to be reported to the legislature regarding the use of the funds is also broad and not necessarily results-oriented. The bill does not provide guidelines or performance requirements by which the effectiveness of the credit can be evaluated such as minimum job creation, new investment, or the stage at which the new commercialized technology is deemed successful.

This is a well-intended bill that would benefit from stronger language defining the use of the tax credit funds toward tech-based economic growth in New Mexico.

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

EWM/blm:svb