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

ORIGINAL DATE 2/5/16
SPONSOR Youngblood **LAST UPDATED** ____ **HB** 276

SHORT TITLE Qualified Business Facility Rehab Tax Credit **SB** ____

ANALYST Graeser

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY16	FY17	FY18	FY19	FY20		
0	>(1,000)	>(1,000)	>(1,000)	>(1,000)	Recurring	General Fund

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	$125.6	$67.9	$67.9	$261.4	Recurring	Taxation and Revenue Department Operating

Parenthesis ( ) indicate expenditure decreases

SOURCES OF INFORMATION
LFC Files

Responses Received From
Taxation and Revenue Department (TRD)
Economic Development Department (EDD)

SUMMARY

House Bill 276 repeals the current Section 7-2-18.4 NMSA 1978, and enacts a new Section 7-2-18.4 NMSA 1978, which provides the qualified business facility construction and rehabilitation income tax credit. The credit is available for taxable years beginning after December 31, 2015 and ending before January 1, 2025, and is available to a taxpayer who owns a qualified business facility and incurs costs to construct, restore, rehabilitate or renovate a qualified business facility and meets other requirements set forth in the section. The credit is nontransferable and is twenty-five percent of the construction costs incurred after December 31, 2015 and before January 1, 2025 to construct a new qualified business facility or fifty percent of the construction cost incurred after December 31, 2015 and before January 1, 2025 to restore, rehabilitate or renovate an existing qualified business facility. However, the credit may not exceed fifty thousand dollars per newly constructed qualified business facility, or one hundred thousand dollars per qualified business facility in the case of restoration, rehabilitation or renovation. A new Section is also added to the Corporate Income and Franchise Tax Act which provides the qualified business facility construction and rehabilitation corporate income tax credit. This credit is for the same time period and at the same percentages as the income tax credit, and is subject to the same limitations. For both credits, a "Qualified Business Facility" is one located in an EDD designated economic development zone or in an Enterprise Zone, also designated by EDD. Apparently, this bill contains the authority for EDD to designate an economic development zone which is required to enable this credit.

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 credit is applicable for construction costs incurred after December 31, 2015 (FY 16) and before January 1, 2025.

FISCAL IMPLICATIONS

EDD notes, "…The bill will result in a reduction in income tax revenues, but will increase gross receipts and other revenues as a result of the construction work performed. Income tax revenues will also increase when the businesses that occupy the buildings constructed begin operating.

New Mexico does not currently have designated enterprise zones, although the Enterprise Zone Act has been on the books since 1993 (Enterprise Zone Act, Section 5-9 NMSA 1978)[1]. According to EDD, "…since 2002, a record 83 New Mexico communities have now passed a Local Economic Development Act (LEDA). Through passing LEDA, a community adopts an ordinance creating an economic development organization and a strategic plan." Apparently, however, none of the 83 communities have availed themselves of the opportunity to designate an Enterprise zone within its strategic plan. This bill would authorize EDD to designate economic development zones under rules promulgated by the Department. Clearly, the economic impact of this bill could range from virtually zero, as is the current experience, to millions of dollars, depending on how extensive or restrictive the economic development zone regulations were. The bill does not constrain the EDD from designating the entire state as an economic development zone and allowing a 25% credit of costs, with a maximum credit of $50,000 per taxpayer per newly constructed facility, or 50% of the costs, with a maximum credit of $100,000 per taxpayer for a renovated or rehabilitated facility.

In either case, it does not appear that there are currently any designated and valid economic development zones extant for which this credit could be claimed.

The existing qualified business facility rehabilitation has seen only three claims for minimal amounts in the previous five fiscal years.

Therefore, qualifying investments cannot be made until additional action is taken by EDD to designate economic development zones or local governments designate enterprise zones pursuant to the Enterprise Zone Act. Thus, the initial fiscal impact in FY2016 & FY2017 is most likely zero.

TRD notes, "… when action is taken to identify revitalization priorities across New Mexico, the fiscal impact can be significant. The bill hints at an aggregate annual limit – Section 1, Para-

[1] http://www.bizjournals.com/albuquerque/blog/real-estate/2016/01/new-proposal-hopes-to-catalyze-enterprise-zones.html

graph, A, Line 7, Page 2 and Section 2, Paragraph A, Line 20, Page 7 – but an aggregate annual limit is not enumerated. Consequently, the per-taxpayer caps ($50,000 new construction or $100,000 renovation/rehabilitation) can quickly escalate to millions of dollars in expenditure."
TRD also notes the following: "The existing law has not been used because New Mexico has not identified enterprise zones for revitalization. However, there exist other construction-related tax relief programs that are currently being used. The current incentives are very specific, are being used, but are not being maximized. The broader opportunity this bill offers will most likely result in maximum participation. For this reason, TRD recommends an aggregate annual maximum for the credit be established."

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

EDD points out that lack of commercial buildings is an impediment to economic development in the state. "The existing Enterprise Zone Act has not been utilized because it calls for municipalities to designate the zones and only allows municipal-level incentives, which municipalities have been unable to afford in recent years. The bill will allow EDD to designate zones, on its own or at the behest of municipalities, and provide a state-level incentive to rehabilitate vacant buildings that blight neighborhoods and add nothing to the tax rolls. The bill will also improve the state's ability to attract new businesses. The lack of available commercial buildings is a regular issue for business consultants and site selectors."

TRD notes the following: "… the bill implicates the tax policy principle of efficiency. From an economic development perspective, it is designed to increase the availability of modernized commercial space in New Mexico. A positive aspect of the bill is that it is tied to zones that either the Economic Development Department, in consultation with other effected agencies, has strategically identified and targeted for redevelopment and revitalization."

LFC staff point out that this bill perhaps places too much authority to create a hit on the general fund in the hands of EDD. Although TRD is required to consult as EDD promulgates rules for designating economic development zones and rules for project approval, EDD has no statutory total tax credit limit to encourage the agency to promulgate limited utilization rules.

PERFORMANCE IMPLICATIONS

The LFC tax policy of accountability is met since TRD is required in the bill to compile an annual report on utilization of the credit and, beginning in 2019 and every two year thereafter, report to an interim legislative committee regarding the data compiled from the reports from taxpayers taking the credit and other information to determine whether the deduction is meeting its purpose.

ADMINISTRATIVE IMPLICATIONS

TRD indicates a “moderate IT impact” that includes upgrades and configuration to IT systems and software. These costs are one-time expenses incurred after bill passage. Future changes will be handled as part of year-to-year transition.

TRD also indicates a minimal administrative impact which includes changes to documents, instructions and forms. Regulation 3.3.13.11 NMAC will need to be reviewed and revised; additional regulations will need to be adopted to implement the new credit, set the application requirements, and define and identify the documentation claimants will need to provide to substantiate entitlement to the credit. The bill does not impact the financial distribution process, but the credit may be subject to the financial disclosure requirements per Governmental Accounting Standards Board (GASB) Statement No.77. GASB 77 disclosure statements 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 will need to be performed by TRD. If the credit meets the criteria, then the disclosure is required in TRD’s financial statements.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

The corporate income tax credit conflicts with Section 7-2A-15 NMSA 1978 which is the Corporate Business Facility Rehabilitation Credit. This bill does not repeal the existing 7-2A-15 NMSA 1978.

SJR 14 and HB 174 work toward allowing local governments to provide ten-year property tax abatements for projects in Enterprise Zones or economic development zones.

TECHNICAL ISSUES

To avoid a run on the general fund that depends on regulatory authority granted to EDD, the statute should be amended to provide an annual utilization cap.

In order to preserve roll-over tax credits, existing 7-2-18.4 NMSA 1978 could be left intact for credits earned prior to the effective date of this bill. Alternatively, section 7-2A-15 NMSA 1978 should be repealed

OTHER SUBSTANTIVE ISSUES

Amounts claimed for exsisting Business Facility Rehabilitation Credit

	FY2010	FY2011	FY2012	FY2013	FY2014
CIT Claims	0	0	0	0	0
CIT Expenditures	$-	$-	$-	$-	$-
PIT Expenditures	$-	$-	$1.0	$-	$-
PIT Claims	0	0	3	0	0

Source: 2015 Tax Expenditure Report

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

LG/jle