

Fiscal impact reports (FIRs) are prepared by the Legislative Finance Committee (LFC) for standing finance committees of the NM Legislature. The LFC does not assume responsibility for the accuracy of these reports if they are used for other purposes.

Current FIRs (in HTML & Adobe PDF formats) are available on the NM Legislative Website ([www.nmlegis.gov](http://www.nmlegis.gov)). Adobe PDF versions include all attachments, whereas HTML versions may not. Previously issued FIRs and attachments may be obtained from the LFC in Suite 101 of the State Capitol Building North.

## FISCAL IMPACT REPORT

ORIGINAL DATE 1/29/16

SPONSOR Strickler LAST UPDATED \_\_\_\_\_ HB 108

SHORT TITLE Rural Infrastructure Tax Credit SB \_\_\_\_\_

ANALYST McIntyre

### REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY16	FY17	FY18	FY19	FY20		
	(\$10,000.0)	(\$10,000.0)	(\$10,000.0)	(\$10,000.0)	Recurring	General Fund

Parenthesis ( ) indicate revenue decreases

### SOURCES OF INFORMATION

LFC Files

#### Responses Received From

Taxation and Revenue Department (TRD)  
Economic Development Department (EDD)

### SUMMARY

#### Synopsis of Bill

House Bill 108 allows a tax credit for a qualified investment in rural New Mexico that produces quantifiable benefits. HB 108 defines “qualified investment” as investment of at least \$1 million in a commercial enterprise project not located in, or within ten miles of, a municipality with a population that is equal to or greater than fifty-five thousand as of the most recent federal decennial census. The enterprise’s purpose must be to manufacture goods for sale; extract natural resources for sale; or process raw materials for sale. The tax credit cannot exceed 30 percent of the cost of the qualified investment, provided that the amount of the credit associated with the purchase of land or fixed assets shall not exceed 50 percent of the amount of the credit associated with the cost of construction of one or more buildings. The investment must include construction for which a loan from a qualified institution has closed.

HB 108 has a tax credit cap of \$10 million per year, allocated on a first come first served basis with a roll-over allowance and not more than three qualified investments from one taxpayer may receive a credit in a taxable year. The Rural Investment Tax credits may be sold, exchanged or transferred to another taxpayer.

The effective date of this bill is July 1, 2016. The delayed repeal date of this bill is June 30, 2026.

## **FISCAL IMPLICATIONS**

It is uncertain how much capital investment in the manufacturing, extraction, and raw materials processing industries occurs each year in rural New Mexico. EDD reported \$8 million in private sector investment in mainstreet districts in 2015, though it isn't clear how much of this investment classifies as in a rural area in the qualified industries. The Encana Corporation invested \$350 million in the San Juan Basin of New Mexico in 2014, according to a presentation given at the July 2014 meeting of the Legislative Finance Committee. Assuming all investments were over \$1 million, were for the purpose of extracting natural resources for sale, included at least one building, and were a quantifiable benefit towards job creation and tax collection, then the rural infrastructure tax credit expenditure would be over \$100 million and be capped at \$10 million in FY15 if it had been in place at the time. Though little to no investment is necessarily expected in 2016 from the extraction industry due to persistently low oil prices, it is not clear when the industry will rebound and resume investment, and so the maximum aggregate tax credit of \$10 million is assumed to be the expected impact of HB 108 in FY17 and beyond.

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**

A rural infrastructure tax credit was recommended by the 2015 Interim Jobs Council.

EDD notes the following issues:

Enacting this tax credit will encourage private investment in manufacturing facilities specifically in rural areas, defined in HB108 as "located in, or within ten miles of, a municipality with a population that is equal to or greater than fifty-five thousand as of the most recent federal decennial census."

TRD notes the following issues:

Serious consideration should be given to the scope this bill and potential overlap with both current and proposed statutes. The bill does not restrict, and in fact appears to contemplate investment by the business itself or its current owners. In that context, and because the bill focuses on manufacturing, the investment tax credit could apply to all or a portion of the same investment. Additionally, the business would benefit the single sales factor phase-in. In an outside investor context, other credits or incentives, such as the Angel Investment Tax Credit, could also apply depending on facts and circumstances. Additionally, several bills have been introduced this session that would provide credits or incentives for facility construction or renovation, adding another layer of potential overlap.

This bill also raises significant concerns regarding simplicity and accountability. There are numerous qualifications that will require taxpayer verification data, provisions that split the credit across multiple tax programs (without an order of preference), and that allow for credit transferability. Taken together both the taxpayer burdens with respect to verification and administration of this credit would be very significant.

As a general rule, TRD does not favor incentives that cross multiple tax programs. If this credit is intended to stimulate outside investment in businesses, income tax credits would suffice. If it is intended to stimulate business expansion, additional consideration should be given to the proposed credit's scope and whether it must straddle tax programs.

### ADMINISTRATIVE IMPLICATIONS

HB 108 mandates that the New Mexico Finance Authority (NMFA) and the Taxation and Revenue department compile a report on a yearly basis. Additionally, it requires the NMFA to certify and qualify eligible projects on forms it creates. It requires promulgation of rules and reporting by NMFA and TRD. Other complex requirements contained in this bill, such as allowing for a carry forward and tracking the completeness or measurable progress of the project will require FTE's and administrative support within NMFA.

TRD notes the following implications:

High impact: In addition to significant one-time expenditures to make IT system enhancements, additional TRD resources will be needed to approve, record, and audit the credits approved, and to manage and record the transfers, and account for the credit across multiple tax programs. A total of 1.5 additional FTE is recommended. The FTE will need to be trained in monitoring the construction and ensuring the project meets the qualifications set by the authority.

Regulations will need to be developed and promulgated, with inter-agency cooperation, along with memoranda of understanding and other agreements that will allow the agencies continued cooperation to account for and track the credit and its recipients.

High IT Impact: Set-up costs within TRD are extensive. They include a one-time investment to update systems and documentation as well as the addition of an FTE.

Estimated Additional Operating Budget Impact*				R or NR**	Fund(s) or Agency Affected
FY2016	FY2017	FY2018	FY 16-18		
154	120	120	394	R	Taxation and Revenue Operating

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

### TECHNICAL ISSUES

TRD notes the following issues:

The language of the bill leaves many elements open to interpretation; regulations and additional definitions should be developed to ensure that claimants apply for the tax credit in a manner

consistent with the intent of the legislation. To promote consistency, regulations and definitions should address the following:

- eligibility criteria, to include, but not limited to, minimum percentage of completion, substantially complete dates that fall outside the time period, the effect of extensions relative to the authorized application period, and any delay attributed to application by the taxpayer;
- management of the secondary market for tax credits created by the transferability of the tax credit:
  - TRD will need to develop procedures to manage transfers;
  - eligibility criteria and limits for the use of acquired transfers;
  - whether transfers can be used in addition to other available credits (ex: rural infrastructure tax credit AND angel investment tax credit);
  - how carry-forward characteristics are handled;
  - whether or not the value of a certificate can be subdivided;
- clarity regarding issuance of the certificate, determination of allocation information, the value of the certificate, extensions, and a standard for “meaningful and measurable progress;” and
- regulations to address the execution of Section K requirements.

Bill language may need to be amended to clarify whether the credit is based upon “the cost of the qualified investment” or the qualified investment only; whether it shall include “land or fixed assets” or land AND fixed assets. These statements results in different valuations for the credit.

It is recommended that the requirements for “rural” be consistent with the requirements for “rural” in existing statutes and regulations, such as the rural jobs tax credit.

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

TM/al